No. _____

In The

Supreme Court of the United States

October Term, 1989

J.M. SMITH CORPORATION, D/B/A SMITH DATA PROCESSING,

Petitioner,

v.

pcI CORP.; HILL PHARMACY GROUP, INC.; KENNETH A. HILL; W.K. ENTERPRISES, INC.; WES KING; RICHIE S. LYNN, D/B/A RICH-2 PHARMACY CONSULTING SERVICES; PROFESSIONAL SYSTEMS S.E., INC.; A. RODNEY ASHBAUGH; DR. T.C. SMITH COMPANY,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fourth Circuit

PETITION FOR WRIT OF CERTIORARI

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April 23, 1990

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QUESTION PRESENTED FOR REVIEW

Did the Court of Appeals err in holding that a party licensed to reproduce a copyrighted work has the right to prepare and publish a derivative work absent authorization to do so?

TABLE OF CONTENTS

TABLE OF CONTENTS – Continued

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

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S.E., INC.; A. RODNEY ASHBAUGH;
DR. T.C. SMITH COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioner, J.M. Smith Corporation, D/B/A Smith Data Processing, respectfully prays that this Court grant a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in this copyright infringement action on December 6, 1989.

OPINIONS BELOW

The opinion of the Fourth Circuit Court of Appeals is unpublished. It is reprinted as Appendix A to this petition at A-3-9.

The opinion of the United States District Court for the District of South Carolina issued on September 1, 1988 and is also unpublished. It is included as Appendix B to this petition at B-1-56.

Petitioner's motion for summary judgment and Respondents' cross-motion for summary judgment were both denied, but the District Court implied a license to reproduce Petitioner's copyrighted work. The motions were decided on August 7, 1987, and the order is reprinted as Appendix C to this petition at C-1-15.

A hearing was held February 18, 1988 upon Respondents' motion for partial summary judgment on the issue of whether or not the right to make a derivative work is automatically conveyed by such implied licensing of the right to reproduce a copyrighted work. The motion was granted at the hearing by oral order. Although a written order was promised at the hearing, it was never forthcoming. The transcript of the motions hearing is reproduced as Appendix D to this petition at D-1-28.

JURISDICTION

The judgment of the United States Court of Appeals for the Fourth Circuit was entered on December 6, 1989. Appellant's Petition for Rehearing with Suggestion for Rehearing In Banc was denied by order dated January 22,

1990, reprinted as Appendix E to this petition at E-1-2. This Petition for Writ of Certiorari is filed within ninety (90) days of that date. The Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

1. EXCLUSIVE RIGHTS IN COPYRIGHTED WORKS: 17 U.S.C. § 106(1) and (2).

> . . . [T]he owner of copyright under this title has the exclusive rights to do and to authorize any of the following:
>
> (1) to reproduce the copyrighted work in copies or phonorecords;
>
> (2) to prepare derivative works based upon the copyrighted work;

2. EXECUTION OF TRANSFERS OF COPYRIGHT OWNERSHIP: 17 U.S.C. § 204(a).

> A transfer of copyright ownership . . . is not valid unless an instrument of conveyance, or a note or memorandum of the transfer, is in writing and signed by the owner of the rights conveyed or such owner's duly authorized agent.

3. OWNERSHIP OF COPYRIGHT: 17 U.S.C. § 201(d)(2)

> . . . The owner of any particular exclusive right is entitled, to the extent of that right, to all of the protection and remedies accorded to the copyright owner by this title.

STATEMENT OF THE CASE*

Smith Data Processing, Petitioner, granted the right to reproduce part of its copyrighted QS/1 pharmacy system to pcI Corp., Respondent, via the license implied by the District Court in the Settlement Agreement. App. C at 10. There was no license or transfer of Petitioner's exclusive right to make derivative works based upon its copyrighted work. Yet, pcI Corp. after settlement enhanced the version of its pharmacy system containing Petitioner's copyrighted work and reproduced and sold such expanded system (Enhanced-pcI). Respondents' enhancements included modules on Nursing Home, Sales Analysis, Patient Counseling, and a Narcotics and Drug Report, all of which appeared for the first time in the pcI product after settlement, much like the addition of chapters to a book. Smith Data Processing sued pcI Corp. for copyright infringement.

The District Court correctly found, as urged all along by Petitioner, that the misappropriation claimed by Petitioner was in part the same misappropriation alleged prior to the Settlement Agreement. Instead of then drawing the proper conclusion that Respondents published an unauthorized derivative work, the District Court concluded that, as a matter of law, the right to make a derivative work is linked to the right to reproduce the copyrighted work, and found no copyright infringement on this issue. The Fourth Circuit affirmed this conclusion.

---

* This action arises under the Copyright Act of 1976, 17 U.S.C. § 101 *et seq.* Pursuant to Rule 29.1, Petitioner states that there are no parent or subsidiary companies of Petitioner J.M. Smith Corporation.

This erroneous conclusion based on the undisputed finding of the fact described above requires review by this Court.

The Derivative Work Issue

The extent to which modifications may be made to a copyrighted work by a licensee who has the right to reproduce the work is a central issue in the developing law of copyright. The integrity of the copyright proprietor's underlying work warrants protection despite market-induced pressure on a licensee to achieve and maintain state-of-the-art status for a product containing the underlying work. For this reason, the Statute (17 U.S.C. § 106(2)) recognizes the right to make a derivative work as a separate right distinct from and in addition to other exclusive rights of the copyright owner.

Amid confusion and disagreement, District and Appellate Courts struggle to comprehend the derivative work issue as it relates to changes which may be made by a copyright licensee to the underlying work. The decision handed down in the present case conflicts with the statute as construed by both Fourth and Ninth Circuit decisions on derivative works. Clarification of the derivative work issue by this Court is critical as we move forward through the age of information.

The Settlement Agreement

Settlement between the parties as to their computerized pharmacy systems *as they existed on May 13, 1983* preceded the coming into being of the cause of action

exerted in this litigation. The cause of action exerted by this litigation arose subsequent to the Settlement Agreement by reason of the post-settlement derivative work created by Respondents.

The release made by Petitioner in the Settlement Agreement did not address possible future derivative works, uncontemplated as of that time. App. F at 6.

Litigation History

On July 23, 1985, Petitioner filed suit in the United States District Court for the District of South Carolina asserting copyright infringement, *inter alia*.

Upon motions for summary judgment, the District Court issued an Order which implied a license in the Settlement Agreement. This implied license sanctioned continued use of Respondents' system as it existed at the time of settlement.[1]

In this same Order on Summary Judgment, the District Court found that:

> . . . [T]he misappropriation which plaintiff claims in this action is, in part, the *same misappropriation* alleged by the plaintiff prior to the settlement agreement.
>
> [emphasis added]

App. C at 9.

---

[1] Although Petitioner believes that the District Court improperly implied the license, it is unnecessary to the presentation of the issue on which review is sought to challenge this conclusion.

In the subsequent Motions Hearing on the derivative work issue, the District Court interpreted the scope of the implied license to go beyond using the underlying work in Respondents' existing system to permit Respondents to make derivative works after settlement. This interpretation was based on the absence in the Settlement Agreement of a statement prohibiting Respondents from creating additional derivative works. The Court stated:

> . . . I do feel as a matter of law the settlement agreement *did not prohibit* the right to make additional derivative works . . .
>
> [emphasis added]

App. D at 27.

Failing to recognize the critical connection between an underlying work and a derivative work thereof, the District Court disposed of the derivative work issue by refusing to consider evidence tendered by Petitioner that Respondents had in fact created a derivative work. That is, no evidence was allowed to show that Petitioner's underlying work was included as part of Respondents' system.

The Fourth Circuit ruled that the derivative work issue was properly resolved by the District Court in its erroneous conclusion which allowed Respondents to make derivative works. Such conclusion, however, was based on a correct finding that the misappropriation following settlement claimed by Petitioner was, in part, the same misappropriation alleged prior to settlement.

ARGUMENT

THE COURT OF APPEALS DEPRIVED PETITIONER OF ITS EXCLUSIVE STATUTORY RIGHT TO MAKE DERIVATIVE WORKS BY AFFIRMING THE DISTRICT COURT'S HOLDING THAT, AS A MATTER OF LAW, THE RIGHT TO MAKE DERIVATIVE WORKS IS LINKED TO THE RIGHT TO REPRODUCE THE UNDERLYING WORK

The Fourth Circuit affirmed the District Court's conclusion in total disregard of the conclusion's direct conflict with the copyright statute and with the Court's earlier decision in *Red Baron-Franklin Park Inc. v. Taito Corp.*, 883 F.2d 275 (4th Cir. 1989).

Copyright Statute

The five exclusive statutory rights in copyrighted works include the right to reproduce the work, 17 U.S.C. § 106(1), and the right to prepare derivative works based thereon, 17 U.S.C. § 106(2).

A written instrument of conveyance is required by Statute to transfer from the copyright owner the particular right to make derivative works. 17 U.S.C. § 204(a).

The owner of any particular exclusive right is entitled, to the extent of that right, to all of the protection and remedies accorded to the copyright owner by Statute. 17 U.S.C. § 201(d)(2).

No License to Create A Derivative Work

Respondents were not licensed to create their post-settlement derivative work of Petitioner's copyrighted underlying work. The erroneous conclusion to the contrary stemmed from an error in reasoning by the Courts

below that *the absence in the Settlement Agreement of a statement expressly prohibiting the creation of derivative works must allow their creation.* Based on this erroneous reasoning, both District and Appellate Courts allowed Respondents to create derivative works, *as a matter of law.* This allowance is an error of law, for it is in direct conflict with the statutory provision *requiring* written conveyance to transfer from the copyright owner the right to make a derivative work.

This error of law is the fulcrum on which this case turns, for it clearly exhibits the failure of the Courts to comprehend the derivative work issue. The error was made out of a misplaced concern by the District Court for recognition of the Settlement Agreement.

Despite the District Court's drive to effectuate the Settlement Agreement, the equities in this case favor Petitioner, as shown below.

Rights Granted by Copyright Are Separate and Distinct

Petitioner relies upon the decision in *Red Baron-Franklin Park Inc. v. Taito Corp.*, 883 F.2d 275 (4th Cir. 1989) which held that the five rights granted to a copyright proprietor under 17 U.S.C. § 106 are separate and distinct, and that the waiver or conveyance of one of the rights does not constitute waiver or conveyance of any other.

In *Red Baron*, the Court of Appeals for the Fourth Circuit, quoting *Columbia Pictures Industries, Inc. v. Aveco, Inc.*, 800 F.2d 59 (3d Cir. 1986), stated:

> The rights protected by copyright are divisible and the waiver of one does not necessarily waive any of the others.

883 F.2d at 280.

Red Baron also recognizes the necessity to license the particular right in question. 883 F.2d at 280. The statutory performance right of Section 106(4), held to be separate and distinct from the other exclusive rights delineated in Section 106, *required* a license in *Red Baron*. License for the performance right was required despite the fact that the selling of a copy of the work was substantially worthless absent the right to use or "perform" it.

In the present case, Petitioner's ownership of the copyrights in QS/1 grants to Petitioner the five separate and distinct rights delineated in Section 106. Relying upon the reasoning in *Red Baron*, the granting of the Section 106(1) right to reproduce Petitioner's underlying work does not also transfer or in any way affect Petitioner's Section 106(2) exclusive right to prepare derivative works based thereon.

Thus, the Settlement Agreement with its implied license to reproduce cannot protect Respondents against infringement of Petitioner's exclusive right to make derivative works. Moreover, the fact that the implied license to reproduce the copyrighted work was derived from a settlement agreement must not serve to extend the rights of Respondents to encompass Petitioner's exclusive statutory right to make derivative works. Even if a written license to reproduce the copyrighted work had been executed, the statutory right to make a derivative work would remain in Petitioner as a separate and distinct right of ownership.

The District Court was in error to allow the creation of a derivative work without benefit of license. The net effect of this error was to permit Respondents to complete

the copying of Petitioner's QS/1 modules and continue to use Petitioner's underlying work in the creation of Respondents' post-settlement derivative work, Enhanced-pcI.

It is imperative that the reasoning leading to this error be scrutinized by this Court.

Petitioner relies further upon the decision in *Oddo v. Ries*, 743 F.2d 630 (9th Cir. 1984), that a license to publish a copyrighted work does not permit the licensee to use that work in a derivative work.

The Court stated:

> . . . [T]he implied license to use the articles in the manuscript does not give Ries or the partnership the right to use the articles in any work other than the manuscript itself. *See Gilliam v. American Broadcasting Cos.*, 538 F.2d 14, 19-21 (2d Cir. 1976) (license to use underlying work in a particular derivative work does not permit licensee to use underlying work in any other derivative work.)

743 F.2d at 634.

Discussing *Gilliam v. American Broadcasting Cos.*, 538 F.2d 14 (2d Cir. 1976), relied upon by the *Oddo* court, Professor Nimmer cited *Oddo* in a footnote to the following:

> Although the *Gilliam* court is not explicit on this point, it apparently reasoned that absent an express authorization to make changes, the license to reproduce and/or perform is limited to reproduction and/or performance in the form in which the authors wrote the work, so that a material departure from such form goes beyond the terms of the license, and hence results in an

> infringement of the reproduction and/or performance rights.

2 *Nimmer on Copyright*, § 8.21[C]

Limited Scope of Implied License

The correctness of Petitioner's reliance on the *Oddo* case is underscored by the decision in *Apple Computer, Inc. v. Microsoft Corp. et al.*, 709 F. Supp. 925 (N.D.Cal. 1989) where the court recognized that a license of sufficient scope is required to authorize the making of a derivative work.

The Court stated:

> . . . [I]t is not reasonable to construe the 1985 Agreement as giving Microsoft . . . an essentially open-ended license to use whatever visual displays its named software could generate in a Macintosh, then or in the future. What Microsoft received was a license to use the visual displays in the named software products as they appeared to the user [at the time of Settlement.]

709 F. Supp. at 929-30.

* * *

> . . . [T]he plain intent and meaning of the 1985 Agreement is to grant a license and release limited to the [version of the programs] as they then existed and appeared to the user.

709 F. Supp. at 930.

The scope of the implied license in the present case was surely limited to future sales of the version of the pcl system in existence at settlement. It was *not* sufficient to license future *versions* of Respondents' system.

A future version of a work *is* a derivative work, and the right to create such requires specific written authorization.

Respondents went beyond the scope of the implied license in creating, reproducing and distributing Enhanced-pcI.

Even without benefit of evidence, both District and Appellate Courts were convinced that part of what was claimed by Petitioner to be misappropriated prior to settlement *was carried forward* in Respondents' post-settlement Enhanced-pcI. App. C at 9; App. A at 7. Having made this finding, it became the duty of the District Court to conclude that Respondents published a derivative work. It was an error of law not to draw this conclusion. Without license to create and publish the derivative work, Respondents infringed Petitioner's copyright in QS/1.

The District Court erred further by not permitting evidence on the derivative work issue and, consequently, improperly disposed of the issue, *despite the finding that part of the claimed misappropriation prior to settlement was carried forward into Respondents' enhanced work.*

The Fourth Circuit concurred with the District Court in both its correct finding and erroneous conclusion. This correct finding of fact by both Courts requires reversal as a matter of law.

CONCLUSION

The decision below formulates legal principles which virtually immunize a licensee from the consequences of modifying a copyrighted work in creating an unauthorized derivative work. The legal conclusions endorsed by the Fourth Circuit transcend the facts in this case and are in direct conflict with established precedents in both another Fourth Circuit panel in the *Red Baron* case and the Ninth Circuit decision in the *Oddo* case. For these reasons, it is respectfully requested that a writ of certiorari should issue to review the judgment and opinion of the United States Court of Appeals for the Fourth Circuit.

Respectfully submitted,

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Attorneys for Petitioner

April 23, 1990

APPENDIX A

FILE COPY

JUDGMENT

UNITED STATES COURT OF APPEALS

for the

Fourth Circuit

FILED DEC - 6 1989

CA 85-1926

No. 88-3181

J M SMITH CORPORATION, d/b/a Smith Data etc. Processing

Plaintiff - Appellant

v.

PC I CORP; HILL PHARMACY GROUP, INC; KENNETH A. HILL; W. K. ENTERPRISES, INC; WES KING; RICHIE S. LYNN, d/b/a Rich-2 Pharmacy Consulting Services; PROFESSIONAL SYSTEMS S.E., INC; A. RODNEY ASHBAUGH; DR. T. C. SMITH COMPANY

Defendants - Appellees

No. 88-3186

J M SMITH CORPORATION, d/b/a Smith Data etc. Processing

Plaintiff - Appellee

v.

PC I CORP; HILL PHARMACY GROUP, INC; KENNETH A. HILL; W. K. ENTERPRISES, INC; WES KING; RICHIE S. LYNN, d/b/a Rich-2 Pharmacy Consulting Services; PROFESSIONAL SYSTEMS S.E., INC; A. RODNEY ASHBAUGH; DR. T. C. SMITH COMPANY

Defendants - Appellants

APPEAL FROM the United States Court for the District of South Carolina.

THIS CAUSE came on to be heard on the record from the United States District Court for the District of South Carolina and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court appealed from, in this cause, be, and the same is hereby, affirmed.

/s/ John M. Graecen
CLERK

UNPUBLISHED

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 88-3181

J M SMITH CORPORATION, d/b/a
Smith Data etc. Processing

Plaintiff - Appellant

versus

PC I CORP; HILL PHARMACY GROUP,
INC; KENNETH A. HILL; W. K.
ENTERPRISES, INC; WES KING;
RICHIE S. LYNN, d/b/a Rich-2
Pharmacy Consulting Services;
PROFESSIONAL SYSTEMS S.E., INC;
A. RODNEY ASHBAUGH; DR. T. C.
SMITH COMPANY

Defendants - Appellees

No. 88-3186

J M SMITH CORPORATION, d/b/a
Smith Data etc. Processing

Plaintiff - Appellee

versus

PC I CORP; HILL PHARMACY GROUP,
INC; KENNETH A. HILL; W. K.
ENTERPRISES, INC; WES KING;
RICHIE S. LYNN, d/b/a Rich-2
Pharmacy Consulting Services;
PROFESSIONAL SYSTEMS S.E., INC;
A. RODNEY ASHBAUGH; DR. T. C.
SMITH COMPANY

Defendants - Appellants

Appeals from the United States District Court for the District of South Carolina, at Spartanburg. Joe F. Anderson, Jr., District Judge. (C/A No. 85-1926-7-17)

Argued: October 2, 1989 Decided: December 6, 1989

Before POWELL, Associate Justice (Retired), United States Supreme Court, sitting by designation, PHILLIPS, Circuit Judge, and HILTON, United States District Judge for the Eastern District of Virginia, sitting by designation.

Ralph Bailey (John B. Hardaway, BAILEY & HARDAWAY, on brief) for Appellant. Mack Ed Swindle (Thomas F. Harkins, Jr., GANDY MICHENER SWINDLE WHITAKER & PRATT, on brief) for Appellees.

HILTON, District Judge:

This appeal and cross-appeal arose out of an action for infringement of copyrights, misappropriation of trade secrets and unfair trade practices, and counterclaims for tortious interference, abuse of process, unfair trade practices, and breach of an earlier settlement agreement. After a bench trial on the merits, the district judge held that a settlement agreement barred all claims of pre-settlement copying, damages proof was too speculative to permit any award, and the state-law claims were preempted. He

found against the defendants on their counterclaims. We affirm.

I.

Plaintiff, Smith Data Processing ("SDP"), began as a wholesale pharmaceutical business in the 1940s. In 1977, plaintiff contracted with a partnership, G & H Limited ("G&H"), for the purpose of converting a computer program previously developed by G&H (QS/1 Pharmacy System) into a program compatible with and run on an IBM Series I computer. The program was to be prepared by SDP, but would be the exclusive property of G&H. After development of this system, SDP sold this system by license from G&H in an assigned territory of the United States. Several of the various sales distributors for the QS/1 system are individual defendants in this case. SDP eventually bought the QS/1 product in 1981.

Prior to this purchase the principals of G&H had begun to develop another pharmacy computer program – the G/H Plus Pharmacy System. There was no mention of this new system in the sales agreement.

With the advent of personal computers, two former employees of G&H, Lyle and Guld, entered into an agreement with G&H for an exchange of technology relating to the G/H Plus product. Lyle and Guld developed a new system compatible with an IBM personal computer and sold all rights to the system to Hill, a former distributor for SDP, who formed the pc I Corporation ("pc I"). Shortly thereafter, upon invitation of Hill, two representatives of SDP viewed the new pc I system. They concluded that it was substantially similar to the QS/1 product. SDP

thus alleged that Hill and pc I were infringing upon a trademark belonging to SDP, were infringing on SDP's copyright, and had misappropriated confidential information belonging to SDP by incorporating certain enhancements of SDP's pharmacy system into the pc I system.

Defendants specifically denied all claims of wrongdoing but agreed to meet with SDP. A settlement was reached on May 31, 1983, in which SDP released pc I, Hill, and their agents, employees, and servants from "any and all past and present claims [SDP] may have against them relating from their individual or collective activities relative to the pc I pharmacy system."

After the settlement agreement was entered into and while it was being consummated, SDP and pc I continued to revise, expand, and market their respective systems. In addition to adding-components to its system, SDP decided to convert its QS/1 system to make it compatible with an IBM personal computer.

In July of 1985, two years after the settlement agreement was entered into, this litigation was instituted. SDP claimed that although the "enhanced" (post-settlement) pc I contains new material which is original to the defendants, it is an unauthorized derivative work of plaintiff's copyrighted expressions of its preexisting QS/1 system. In addition, SDP claimed that additional causes of actions stemmed from these basic contentions. Defendants, on the other hand, asserted that the only new claim advanced by the suit was copying as to one specific portion of the program and that all other claims were governed by the settlement agreement. They argued that the suit

was brought merely to interfere with pc I's competitive advantage in the pc pharmaceutical market.

II.

In the initial summary judgment order, the trial court ruled that the settlement agreement barred any claim for copyright infringement which occurred prior to the date of the settlement agreement. At the conclusion of the bench trial, the court found that post-settlement copying had occurred as to one portion of the program but not as to any others, and that the federal copyright statute pre-empted appellant's trade secret claim. The court refused to award damages finding the proof too speculative and issued injunctive relief to cover the copied portions of the program.

The counterclaims were resolved against the defendants on the findings that the action was brought in good faith and that plaintiff had not breached the settlement agreement.

III.

On appeal, appellant contends that the settlement agreement reached between the parties does not extend to derivative works of the program that existed at the time of settlement. This issue was properly resolved in the summary judgment finding that the misappropriation which plaintiff claimed was, in part, the same misappropriation alleged by the plaintiff prior to the settlement agreement.

Appellant further contends that the findings as to post-settlement copying were clearly erroneous. This claim must be rejected. The trial court was in the best position to make determinations as to whether or not copying had occurred. There was ample evidence to support the decision, and this court will not disturb the judge's factual findings. *See Anderson v. City of Bessemer*, 470 U.S. 564, 573-74 (1985).

Appellant also complains that the trial court erroneously excused Hill's secrecy obligation to SDP. Appellant fails, however, to explain why, based on its assertions as to the copyrighted nature of the material allegedly misappropriated or misused, the rule of federal preemption of copyright claims would not control. *See Del Madera Properties v. Rhodes and Gardner, Inc.*, 820 F.2d 973, 976-77 (9th Cir. 1987); *Videotronics, Inc. v. Bend Electronics*, 564 F. Supp. 1471 (D. Nev. 1983).

Finally, appellant asks for a remand on the issue of damages and injunctive relief. This court finds that there was ample evidence to support the ruling on these issues.

On cross-appeal, appellees assert error in the finding that plaintiffs did not breach the settlement agreement, and argue that plaintiff's persistence in prosecuting this action demonstrates an abuse of process. They further assert that they are entitled to attorneys fees for their defense of the infringement claim. This court has considered the claims and finds appellees' argument to be without merit.

As there was ample evidence to support the findings and conclusions in this case, we affirm without further

discussion of the issues on the well-reasoned opinion of the district court.

AFFIRMED

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
SPARTANBURG DIVISION

J M Smith Corporation, d/b/a Smith Data Processing, Plaintiff,	)	C/A 7:85-1926-17
vs.	)	ORDER
pc I Corp., Hill Pharmacy Group, Inc., Kenneth A. Hill, W. K. Enterprises, Inc., Wes King, Richie S. Lynn, d/b/a Rich-2 Pharmacy Consulting Services, Professional Systems S.E., Inc., A. Rodney Ashbaugh, and Dr. T. C. Smith Company, Defendants.	)	FILED SEP 01 1988

This is an action for the alleged infringement of copyrights on a computer program designed to enhance the efficient management of a pharmacy. In addition, plaintiff asserts causes of action for misappropriation of trade secrets and unfair trade practices. The defendants deny infringement, set up various affirmative defenses, and have counterclaimed alleging acts of tortious interference, abuse of process, unfair trade practices, and breach of an earlier settlement agreement.

PROCEDURAL HISTORY

Plaintiff previously moved for summary judgment on Count I and Count III of the complaint. This motion was denied in an order dated August 7, 1987. However, the court did determine, in accordance with Rule 56(d), *Fed. R. Civ. P.*, that the following material facts existed without substantial controversy:

(1) Plaintiff is the owner of all right, title and interest in and to the QS/1 Pharmacy System, including all copyrights therefor; and

(2) Plaintiff is the owner of copyright registration TXu 189-270 and supplemental copyright registration TXu 197-301; and

(3) Said copyrights are valid.

See order dated August 7, 1987.

The defendants also moved for summary judgment, contending that an earlier settlement agreement between the parties extinguished all of plaintiff's claims in this case. While denying defendants' motion, the court did find that the following material facts existed without substantial controversy and would be deemed established at trial:

(1) The settlement agreement dated May 31, 1983, bars any claim for copyright infringement which occurred prior to the date of the settlement agreement; and

(2) Any act or acts of infringement occurring after May 31, 1983, including specifically any acts of infringement relating to the Drug Interaction and Patient Counseling Data and any infringement occurring after May 31,

1983 relating to any enhancements to the QS/1 Pharmacy System, are actionable. *See* order dated August 7, 1987.

Subsequent to the August 7 order, the defendants sought clarification from the court regarding the question of whether the pc I system was a derivative work of plaintiff's system. The court ruled from the bench February 18, 1988 that the settlement agreement precluded plaintiff from showing that pc I with modifications made after settlement constitutes a derivative work unless such modifications contain copyrighted material copied from QS/1.

Prior to trial, plaintiff announced that it would abandon certain of its claims, including its claim for violation of 18 U.S.C. § 1961, the Racketeer Influenced and Corrupt Organizations Act.

As a result of the court's orders and plaintiff's stipulation regarding certain of its claims, plaintiff's case includes, in addition to Count III (Infringement of Patient Counseling Data Copyright) which is viable in its entirety, the following counts which are limited to wrongful acts occurring after settlement:

Count I - Infringement of Program Copyrights;

Count II - Infringement of Screens Copyrights;

Count XI - Unfair Trade Practices under the South Carolina Unfair Trade Practices Act; and

Count XII - Misappropriation of Trade Secrets.

This matter was tried by the court without a jury on March 14-18, 21, 22 and 28, 1988 in Greenville, South Carolina. The court heard oral arguments on March 28,

1988, and counsel have filed post trial memoranda. Additionally, four telephonic conferences were conducted, at the request of the court, in order to allow additional oral argument on certain issues which were deemed particularly important.

After receiving the testimony, carefully considering all the evidence, weighing the credibility of the witnesses, reviewing the exhibits and briefs, and studying the applicable law, this court makes the following Findings of Fact and Conclusions of Law pursuant to Rule 52 of the *Fed. R. Civ. P.* The court notes that to the extent any of the following Findings of Fact constitute Conclusions of Law, they are adopted as such, and to the extent any Conclusions of Law constitute Findings of Fact, they are so adopted.

FINDINGS OF FACT

The Parties

Plaintiff J M Smith Corporation, d/b/a Smith Data Processing ("SDP") is a corporation organized under the laws of the State of South Carolina, with its principal place of business at Spartanburg, South Carolina.

Defendant pc I Corp. is a Texas corporation with its principal place of business at Granbury, Texas.

Defendant Hill Pharmacy Group, Inc. is a corporation organized and existing under the laws of the State of Texas, having a principal place of business at Granbury, Texas. Hill Pharmacy became a distributor of the QS/1 Pharmacy System in 1981.

Defendant Kenneth A. Hill is a resident of the State of Texas, residing at Granbury, Texas. Mr. Hill was the owner of the Hill Pharmacy Group, Inc. On behalf of Hill Pharmacy, Mr. Hill signed a license agreement with plaintiff in 1981, and Hill Pharmacy Group, Inc. thereupon became a distributor of plaintiff's QS/1 Pharmacy System.

Defendant W. K. Enterprises, Inc. is a corporation organized and existing under the laws of the State of Kansas, having a place of business at Joplin, Missouri. W. K. Enterprises, Inc. became a distributor of the QS/1 Pharmacy System in 1981.

Defendant Wes King is a resident of the State of Missouri, residing at Joplin, Missouri. King is an owner of W. K. Enterprises, Inc. On behalf of W. K. Enterprises, Wes King signed a license agreement with plaintiff in 1981.

Defendant, Richie S. Lynn, d/b/a Rich-2 Pharmacy Consulting Services, is a resident of the State of New York, residing at Owego, New York. Lynn is an owner of the business trading under the name Rich-2 Pharmacy Consulting Services. On behalf of Rich-2 Pharmacy Consulting Services, Lynn signed a license agreement with plaintiff in 1981, and Rich-2 Pharmacy Consulting Services thereby became a distributor of the QS/1 Pharmacy System. In addition, Lynn worked as a pharmacist in his father's drug store, known as "Lynn's Drug Store," which was a licensed end-user of the QS/1 system.

Defendant Professional Systems, S.E., Inc. is a corporation organized and existing under the laws of the State of Florida, having a place of business at Boca Raton,

Florida. Defendant A. Rodney Ashbaugh is an owner of Professional Systems, S.E., Inc. On behalf of Professional Systems, S.E., Inc., Mr. Ashbaugh signed a license agreement with plaintiff in 1981, and Professional Systems, S.E., Inc. became a distributor of the QS/1 Pharmacy System.

Defendant A. Rodney Ashbaugh is a resident of the State of Florida, residing at Boca Raton, Florida. In addition, Mr. Ashbaugh is an owner of a local drug store in Boca Raton, Florida, known as "Community Pharmacy," which was a licensed end-user of the QS/1 system.

Defendant Dr. T. C. Smith Company is a corporation organized and existing under the laws of the State of North Carolina and having a place of business at Asheville, North Carolina.[1]

Defendants, Ken Hill, Richie Lynn, and Rod Ashbaugh are each stockholders and members of the board of directors of the pc I Corp. Messrs. Lynn, Ashbaugh, and King are each regional managers of defendant pc I Corp.

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[1] The allegations concerning defendant Dr. T. C. Smith Co. differ slightly from the allegations regarding the remaining defendants. Plaintiff contends that Dr. T. C. Smith Co. violated its copyrights by distributing infringing works. Plaintiff makes no allegation that Dr. T. C. Smith Co. participated in any of the alleged copying activities of the other defendants. Since the evidence clearly indicates that Dr. T. C. Smith Co. distributed the pc I system, the liability of this defendant need not be considered separately from the other defendants. If plaintiff's system has been copied, Dr. T. C. Smith Co. would be liable along with the other defendants. If, however, no copying is shown, Dr. T. C. Smith Co., as well as the other defendants, would not be liable for copyright infringement.

and oversee sales distribution of the pc I Pharmacy System in their respective geographical regions. Defendants Lynn, Ashbaugh, and King perform their sales and distribution duties for pc I Corp. through their respective businesses, namely, defendants Rich-2, Professional Systems, and W. K. Enterprises. Hill is the president of pc I Corp., and King is a member of the board of directors of pc I Corp. Dr. T. C. Smith Co. is a Wholesale Drug Affiliate of pc I Corp. and sells the pc I Pharmacy System under a sales commission agreement. Sales of the pc I system are made by the Dr. T. C. Smith Co. in South Carolina.

Product History

A brief history of the QS/1 product and the pc I product is necessary to an understanding of how this dispute arose. Plaintiff began operation as a wholesale pharmaceutical business in the 1940's. In 1977, SDP contracted with a partnership known as G&H Limited for the purpose of converting a computer program previously developed by G&H into a program compatible with and to run on an IBM Series 1 computer.[2] The program was to

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[2] The Series 1 computer is a mini computer. The personal computers, which are popular today, are called micro computers. Mini computers are much larger and more expensive than personal computers and are used exclusively in business settings. Until 1982 micro computers were generally not used in the business setting because they lacked sufficient memory capacity. In 1982, IBM introduced an improved line of micro computers which had sufficient memory capacity to make the micro computer an attractive alternative in the business setting.

be prepared by SDP, but would be the exclusive property of G&H. The system developed under this arrangement between SDP and G&H has gone by various names at various times but is now commonly referred to as the QS/1 Pharmacy System or "QS/1".

After the development of QS/1, SDP, by license from G&H, sold the system as a distributor in an assigned territory in certain states including South Carolina. The defendants in this case likewise were distributors of QS/1 when it was owned by G&H. On June 22, 1981, G&H and SDP entered into an agreement by which the then existing QS/1 system was sold to SDP.

Prior to the sale of QS/1, the principals of G&H had begun to develop another pharmacy system which is commonly referred to as the "G/H Plus Pharmacy System" or "G/H Plus". There was no mention of G/H Plus in the June 22, 1981, Sales Agreement, and it is admitted by SDP that it did not purchase any rights to G/H Plus. In fact, no complaint has been made with respect to G/H Plus, and as stipulated by SDP's counsel during the trial, there is no complaint that the authors of the pc I system copied G/H Plus.

Following the June 22, 1981 agreement, many of the distributors of QS/1 became distributors for SDP, the new owner of QS/1. These distributors executed license agreements authorizing them to use and sell the QS/1 system. These distributors were independent contractors for SDP and were not employees.

After distributing plaintiff's product and experiencing market developments, some of the defendants concluded that a lower cost product was needed to meet

competition in the pharmacy computer system marketplace. The advent of the IBM personal computer in 1982 provided added incentive for a pharmacy system which could be run on a micro computer such as the IBM personal computer.

In January of 1982, Ken Hill had a discussion with Jim Smith, Chairman of SDP, in which Hill told Smith that it was crucial for the distributors to have a low priced pharmacy system such as one that would run on the new IBM personal computer. Smith told Hill in January of 1982 that SDP did not intend to redesign its product to be capable of running on a personal computer since he, Smith, did not believe the personal computer to be a serious business machine. Hill disagreed with Smith and told him that if SDP would not provide a pharmacy system to run on a micro computer at a lower price than the QS/1 system, the distributors would have to have an alternate product to serve as an entry level system and that he, Hill, would attempt to locate such a product.

During 1982, Hill began to look for an alternate pharmacy computer system to serve as an entry level product. After considering, and rejecting, two other entry level systems, Hill became aware of a software product which had been written by Mark Lyle and Barry Guld in Canada. Hill examined this system in January of 1983.

Lyle and Guld were former employees of G&H and sought to capitalize upon the trend to smaller computers by entering into an agreement with G&H for an exchange of technology relating to G/H Plus. Using the G/H Plus, Lyle and Guld developed a pharmacy program which was compatible with an IBM personal computer.

When Hill saw the product that had been developed by Lyle and Guld and their corporation, Zadall, Hill formed a Texas corporation, pc I Corp. to begin efforts to market the new product. Hill's new corporation purchased all rights to the new pharmacy system from Lyle, Guld and Zadall and named the new product, pc/1. pc I Corp. purchased the rights to the pc/1 product (now known as the pc I product) in February of 1983 by issuing two-thirds (2/3) of the stock in pc I Corp. to Lyle and Guld. Later, pc I Corp. repurchased from Lyle and Guld for a substantial amount of cash the shares of stock in pc I Corp.

The Earlier Dispute and Resulting Settlement

In the Spring of 1983, Ken Hill was demonstrating the new pc/1 product at a meeting of the American Pharmaceutical Association in New Orleans. Various representatives of SDP, including Ken Couch and Bill Cobb, viewed the system demonstrated by Hill. Hill had actually invited Couch and Cobb to see the system and had made no effort to hide or disguise the system.

When Couch and Cobb saw the system, they became angry and believed at that time that the pc I system had been copied from QS/1. Neither Couch nor Cobb were familiar with the G/H Plus product and did not know the common heritage of the pc I system and QS/1. After Couch and Cobb saw the pc I system, SDP instructed its legal counsel to send a demand letter to Ken Hill and pc I Corp. The demand of SDP, in part, alleged copyright infringement and misappropriation of confidential information. The demand also alleged that Hill and pc I Corp.

were infringing upon a trademark belonging to SDP and demanded that Hill and the defendants recall all of the pc I systems and "remove all confidential, proprietary and/or copyrighted information therefrom."

A settlement conference was held in Fort Worth, Texas in May of 1983, and during those negotiations, the parties reached an agreement. This settlement agreement was drafted by legal counsel and ultimately signed on August 16, 1983, but by its terms it provided it was "entered into as of" May 31, 1983.

Under the settlement agreement, SDP released pc I Corp., Hill, and their agents, employees and servants from any and all past and present claims that SDP might have against them arising out of their individual or collective activities relative to the pc I Pharmacy System. Additional provisions of the settlement agreement required SDP to assign in blank its stock in UDA, Inc., a corporation established by distributors of the QS/1 system for the purpose of distributing certain IBM hardware. The settlement agreement also required that Hill and the defendants cancel certain maintenance agreements they had with end users of the QS/1 product and to relinquish annual fees which they enjoyed from those maintenance contracts. In addition the defendants agreed to change their trademark from pc/1 to pc I.

In the months following May 31, 1983 and the execution of the settlement agreement on August 16, 1983, the parties performed basically all of the requirements of the settlement agreement. The final step required by the agreement occurred on January 17, 1984, when SDP forwarded, through its legal counsel, the shares in UDA

which SDP had agreed to transfer in blank. The cover letter accompanying this stock indicated that both sides to the agreement had "concluded the various tasks" to be performed under the agreement and indicated that the matter was closed.

This settlement agreement formed the basis for the defendants' motion for summary judgment and this court's order of August 7, 1987, which held that acts of infringement, if any, which predated the settlement agreement were not actionable.

After the settlement agreement was entered and while it was being consummated, SDP and pc I continued to refine, expand, and market their respective systems. In addition to adding components to its system, SDP, apparently having determined that Smith's earlier prediction about the personal computer was inaccurate, decided to convert its QS/1 system to make it compatible with an IBM personal computer.

Stipulations and Definitions

Because the date of the settlement agreement (May 31, 1983) is the "watershed" date for determining whether impermissible copying has occurred, any analysis of whether there has been a copyright violation should begin by focusing on which components were in the defendants' system as of this critical date. The court's task in this regard has been made easier by reason of certain stipulations made by the parties to this action.

Specifically, the parties stipulated that the pc I system contained the programs of prescription processing and

and application, patient profiles, system tailoring (also called the store file), the ability to print labels and multiple labels, reports and help screens. The parties also stipulated that the pc I system, on May 31, 1983, did not contain its nursing home module and sales analysis module. Rather, the nursing home module, though under development, was not attached to the pc I system until late 1983, and the sales analysis module was attached to the pc I software in early January of 1984. The parties did not stipulate as to when patient counseling codes were written in the ancillary drug list, or when the pc I system had the capability to use the patient counseling codes from the ancillary drug list. There was also no stipulation as to when a certain narcotic and controlled drug report was available in the pc I system.

Based on the above stipulations, much of the evidence at trial related to the nursing home and sales analysis modules, the ancillary drug list's patient counseling codes and a single report, referred to as the Narcotic and Controlled Drug Report.

The QS/1 Pharmacy System which is in question in this action is commonly referred to in the computer industry as application software. The application software, working together with the operating system and the computer hardware, causes the computer to display screens of information on the cathode-ray-tube or the screen. This permits the end user, in this case a pharmacist, to input information or data into the storage facility of the computer hardware, to be stored until needed. Additionally, the user may cause an output of that data or information by way of a display on the screen or a printer connected

to the computer's central processing unit. The application software controls all of these functions.

Application software is expressed in written form in source code. That source code is written by a programmer and can be written in a number of different languages, such as "Basic", "FORTRAN", and "Assembler". The QS/1 software is written in a language that is proprietary to SDP and is not commonly known among other programmers. The application software referred to as the pc I system is written in a different language from that of QS/1. SDP admits that the pc I programmers have never had access to the QS/1 source code. Accordingly, there is no complaint in this action by the plaintiff that pc I's source code is copied from QS/1's source code.

With respect to the alleged infringement of the QS/1 program and screens, SDP's evidence consists almost entirely of plaintiff's Exhibit 10, which provided side by side comparisons of various screens from the systems in question. The court admitted Exhibit 10 over the objection of the defendants. The first seventy-six (76) pages of Exhibit 10 related to components of the system prior to the May 31, 1983 settlement agreement. Accordingly, only pages 77 and following were considered as to plaintiff's claim of infringement.

Copyright Infringement

Count I of the complaint alleges infringement of plaintiff's QS/1 computer program by defendant's pc I program. Count II is directed to the texts appearing on screens generated by the program. Asserted in Count III

is infringement of plaintiff's QS/1 Drug List and Patient Counseling Data.

Access

Defendants Ken Hill, Wes King, Richie Lynn and Rodney Ashbaugh were distributors of QS/1 prior to settlement. Defendants Hill, Lynn and Ashbaugh were end-users of QS/1. The expressions and flow allegedly copied into pc I were in QS/1 at the time defendants were distributors and end-users. Defendants also had access to the confidential and proprietary information of plaintiff through the distributor relationship.

Plaintiff's Exhibit 31 is a letter dated March 27, 1984 from former QS/1 distributor Richie Lynn to Richard Gobin, a QS/1 (PDQ) end-user. The following excerpt is a pertinent portion of the letter:

> *We have designed the pc I system so that it would perform all tasks that the QS/1 would handle* and then proceeded to add all those extras we had been seeking for a number of years. The following is a partial list of enhancements performed by pc I *that are not in the present or next scheduled enhanced release of PDQ.*
>
> * * *
>
> We can produce the same sheets as you are now currently producing, *or those capable of being produced by PDQ,*. . . . [Emphases added.]

Mr. Lynn's letter indicates how intimately familiar he was with QS/1 almost ten months after his distributorship agreement was terminated, to the extent that he knew what would be included in future releases of QS/1.

The distributorship and end user agreements, together with the letter set forth above, compels the court to find that defendants had the requisite access to the plaintiff's system. Having determined that the defendants had access to the expressions allegedly copied into pc I, the court now proceeds to determine whether substantial similarity exists between the two systems.

Substantial Similarity

Nursing Home Component

Many pharmacy systems, including QS/1, provide a means by which nursing homes monitor drug information as well as other medical needs of each patient. A drug order is a medication prescribed for a patient. Non-drug orders include instructions concerning diet, treatments, lab instructions and physical therapy.

Prior to September 1981, the QS/1 system included a Basic Nursing Home component. In September of 1981, defendant Hill held a meeting at his offices in Granbury, Texas to determine what features would be needed in a pharmacy computer system for a pharmacy to more effectively serve a nursing home. The Granbury meeting was attended by some persons who were users or distributors of the QS/1 system. It was also attended by others who were experts in the nursing home field who were not associated in any way with plaintiff or the QS/1 system.

Hill made hand written notes at and following that meeting and asked Max Gregory to take the minutes of the meeting for him. Hill also obtained commonly available information on other pharmacy nursing home computer systems. At the time Hill did so, he was an

independent distributor of the QS/1 product. He furnished copies of his notes and information to the programmers at SDP to permit SDP to incorporate his ideas into the QS/1 system. Each of the six (6) similarities in the pc I and QS/1 nursing home components were addressed in the notes of Ken Hill.

Plaintiff's Exhibit 11 contains an assortment of documents that defendants assert they relied upon in the development and implementation of pc I. Included as Exhibit 11-F is a report of the Granbury meeting held in September, 1981, which includes recommendations for entering non-drug orders into the QS/1 system. The recommended approach involves an arrangement analogous to a wall divided into "pigeon holes". A number of such pigeon holes are collected into groups, each representing a type of non-drug order, as seen on page 7 of plaintiff's Exhibit 11-F. Types of non-drug orders listed include routine orders, diet, physical therapy, nurses orders, lab, comments and treatments. Orders of the same type would be stored in the same group of pigeon holes for each patient.

The QS/1 programmers rejected the recommendation of the Granbury meeting. Instead, they recognized a commonality between the different type of orders and entered them in a manner analogous to writing a message on a single page, continuing to use additional pages as required. Each single page provides adequate space for a complete message and the number of messages is limited only by the space in the entire Sig File where these non-drug orders are hidden. Orders of all types, received in random sequence, can be entered into the system in that same sequence. The QS/1 system assigns a code to the

page carrying the message which identifies the order according to type. The applicable patient is associated with the order entry, although the patient's name does not show on the screen. The sorting capabilities of the computer may then be relied upon to group the orders according to any desired scheme after they have all been entered in one file.

The pc I programmers also rejected the recommendations of the Granbury meeting for implementing non-drug orders and instead utilized a method not unlike the QS/1 system. A two-line entry format is referred to in plaintiff's Exhibit 10, the purpose of which is to indicate provision of adequate space for an order of any kind. Pc I added the ability to show the pharmacist how the two lines could be broken up into four lines by putting dots in the middle. This break only occurs when non-drug orders are printed down the left-hand side of a form such as a physician's order form or a treatment sheet. The dots in the pc I format indicate to the pharmacist where his message will break to conform to the blocks of information on the printed form. Regardless, the entry format is two lines for both systems. It is important to bear in mind, however, that the two-line format is not the salient feature of the non-drug order entry. The important feature is the expression utilizing the single page analogy as opposed to the pigeon hole analogy.

G/H Plus does not have a separate non-drug order entry screen and, therefore, pc I could not have utilized G/H Plus' methodology.

There are different types of non-drug orders, including diet, treatment, physical therapy and lab. It is helpful

to a nursing home to have the same type orders grouped together on the printed forms for each patient. It is also advantageous to be able to print out all the entries for one type order. QS/1 developed one position type codes to identify the types of non-drug orders, including the following:

D – Diagnosis

L – Lab

F – Diet

P – Physical Therapy

T – Treatment

In all instances except one, the type code corresponds to the first letter of the order description, but in the case of "Diet", the letter "F" was used because the letter "D" was previously assigned to "Diagnosis". These designations are also in accordance with the Granbury report. In defining the codes in the pc I type field, pc I programmers included "F" for "Diet" even when "D" was available to them to use.

G/H Plus does not utilize a type field, and therefore pc I did not derive its type code from G/H Plus.

When SDP programmed its nursing home modules into the QS/1 system, its programmers worked closely with Ken Hill and utilized a number of the features Hill had requested to be in the QS/1 nursing home package. Later in 1983, when Hill was assisting the programmers of the pc I Pharmacy System in designing a nursing home module, Hill used some of the ideas and features he had earlier compiled. SDP claims that Hill, by furnishing the ideas for features in a nursing home package to SDP,

prevented himself from later using those ideas in any other system. However, the court finds that there is nothing, by way of agreement or otherwise, that prevents Hill from using his notes, the ideas and features he had compiled and his own ideas and concepts in the design of the nursing home module of the pc I product. Hill was never paid any consideration for holding the Granbury meeting nor for his ideas or efforts in designing a nursing home component that could be used in conjunction with the QS/1 system.

Present also at the Granbury meeting was a man by the name of Vogle who had worked on and designed another nursing home system. Vogle provided information about that system to Hill and the others at the Granbury meeting. Some of Vogle's ideas were actually used in the nursing home module of the QS/1 system. Vogle also provided UDA with certain forms which could be used in conjunction with the QS/1 nursing home programs. One of these forms appeared as a part of plaintiff's Exhibit 10, and SDP claimed that pc I's use of this form somehow infringes on QS/1, because the QS/1 form does not appear in the G/H Plus manual. The form does not contain a copyright notice by SDP or anyone else.

The court finds that the use by pc I of this form is with the permission of UDA, and that there is no evidence to support any claim of copyright infringement with respect to this form.

The Hours of Administration (HOA) codes are abbreviations for the time(s) that medication (and in some cases non-drug orders) is to be administered to a patient.

The HOA table is that part of QS/1 where the user sets up the codes and defines them to the system. The codes are then attached to the prescription orders and are printed out on the chart of a patient. This service is of particular importance to the nursing home, and thus to the pharmacist, because a nurse or attendant can readily see when each medication is to be administered.

The QS/1 HOA table consists of the HOA code, a one-position frequency code, and eight slots or columns of four positions each where the applicable times of day for administering medication are recorded.

The implementation of HOA in both QS/1 and pc I, while generally following the Granbury recommendations, differs from those recommendations with respect to the frequency code. The Granbury participants assigned frequency codes sequentially to the medication entries. The actual use of the frequency code in QS/1 is to indicate the number of times each day the particular medication must be given. The QS/1 system can then sort and print medications and certain non-drug orders according to frequency, thus making the nurses' job much easier. This change made by QS/1 is also seen in the pc I system.

The HOA code can work in conjunction with the non-drug order entry feature. An HOA code, e.g. "8D", may appear with the entry "turn patient in bed". The HOA table (screen) may show "8D" referring to eight times a day, and the hours for effecting the order are indicated. Thus, the nurse is reminded to turn the patient in bed at certain times and can initial the chart to indicate completion of the task.

G/H Plus does not have an HOA field. It uses the frequency field for placement of the medications on charts rather than as an indicator of the number of times per day the medication is to be administered. Also, G/H Plus has only four different times of administration that can be set up for a particular frequency.

QS/1 Pharmacy System does not have a separate nursing home file. Designing a separate file, while being the straightforward approach for incorporating nursing home information into a computer system, is an involved process. Additional programs are required for setting up and maintaining each separate file, including programs to make a security back-up for the file, and to list, print, clear, and reload the file. A separate file further necessitates having separate screens to display information entered, stored and retrieved. Because the features of QS/1's nursing home components lend themselves to being incorporated into existing QS/1 files, and due to the time and effort involved in designing a separate file, plaintiff decided against a separate nursing home file.

QS/1 stores each nursing home as if it were a patient along with the nursing home descriptive information in its patient file. Since both nursing homes and patients have a name, address, etc., this manner of storage is a logical way of setting up the nursing home particulars. Pc I likewise stores each nursing home as a patient in its patient file, along with the nursing home information. Hill testified at trial that the reason for pc I doing so (other than its being a reasonable approach, which plaintiff maintains is 20/20 hindsight) was because the pc I programmers did not want to create another file due to a twenty-file limit to their system. This implementation is

unlike that in the G/H Plus system, which stores nursing home information in a vendor file, and therefore this feature in pc I was not derived from G/H Plus.

Patient information relating to a nursing home patient is stored in QS/1 in the patient record of the patient file. Since each nursing home is treated as a patient, nursing home information is likewise stored in its own "patient" record in the patient file, hereinafter referred to as the nursing home record. A patient's record is then linked to the applicable nursing home record.

Most nursing home patients have their own primary physician. The QS/1 system stores the primary physician code in the patient record. The house physician of a nursing home is stored by QS/1 in the nursing home record. The house physician serves as an alternate physician to patients who designate a primary physician, but is many times a patient's only physician.

While this method may be imperfect, the pc I system stores the code for the primary physician in the patient record of the patient file end the code for the house physician in the nursing home record of the patient file in the same manner as QS/1.

G/H Plus does not maintain the code for the house or alternate physician in the nursing home record, and therefore this feature in pc I was not derived from G/H Plus.

SDP relies heavily upon the fact that the six (6) features in the nursing home module about which they complain are not similar to the G/H Plus product but are similar in the pc I and QS/1 products. There is evidence

that some of the contested features of pc I are similar to or derived from G/H Plus. However, the degree of participation of the defendant Hill in the design of both pc I and QS/1 persuades the court that the fact that the nursing home module in pc I differs in part from G/H Plus is not indicative of copying. Many of the ideas in the pc I nursing home module were ideas which the defendant Hill had compiled over the years, beginning in 1981.

SDP contends that the notes Hill made of the Granbury meeting were confidential information belonging to SDP. The license agreement to which Hill's company was a party at the time of the Granbury meeting provided as follows:

> The copyright, and the ideas and expressions thereof contained in the System, and all physical embodiments thereof, and materials supplied hereunder in connection therewith, are acknowledged by Licensee to be confidential, proprietary information. Licensee will not provide or make available to others than the End-User and those of its employees required to use the System in its business, the System, or any part thereof, including any physical embodiment thereof, or any materials supplied by SDP in connection therewith, including but not limited to flow charts, logic diagrams and source code, in any form. Licensee shall take all steps necessary to protect the confidentiality of the System and the rights of SDP.

The licensee agreement thus provides for confidentiality of "*the* copyright," and "*the* ideas and expressions *thereof*" as well as "materials *supplied* hereunder." It does not address ideas or suggestions of the licensee, who is therefore entitled to reuse, for his own benefit ideas,

expressions and features as well as his notes with respect to the nursing home module.

Hill used his ideas and features, as well as his notes, when he, in conjunction with the programmers, designed the nursing home module of the pc I System. Accordingly, although certain features of the two systems do appear to be similar, defendants have met their burden or rebutting the presumption of copying raised by proof of access and similarity.

Sales Analysis Component

Most pharmacy computer systems have the capability of providing a daily report to the pharmacist which gives a record of prescription activity and reflects profit and loss figures for the day. The sales analysis report, however, is a special report which serves as an extensive management tool rather than as a simple daily report. The report not only summarizes daily sales but can present them according to specified price ranges and indicate total activity (number of prescriptions filled and dollar amounts) for each price range. In analyzing prescriptions according to price range, the pharmacist is able to see which ranges are bringing a profit so that pricing strategy may be adjusted if required to insure profitability. Sales analysis is also used, for example, to analyze third-party (insurance) plans, a particular group of patients at a nursing home, sales per group or sales per selected time period, and many other pertinent categories.

The range feature is the critical item in sales analysis. The remaining items could appear in a variety of financial reports. But in QS/1 sales analysis, the interplay between price range and the remaining items presents a unique analysis of information.

SDP has complained that pc I has copied this report which QS/1 calls its Prescription Sales Analysis. SDP admitted that its QS/1 system does not contain a sales analysis module, but simply contains a program which has the capability of printing one or two reports for a pharmacist to use in analyzing sales. By contrast, the pc I product has an entire sales analysis module consisting of four (4) menu selections, multiple screens of sales data, graphic capabilities and printed reports.

SDP has admitted that the sales analysis module of pc I was not copied from QS/1. Rather, SDP limits its claim in this regard to the allegation that pc I simply copied the format of a single report.

The allegedly infringing report isolated by SDP has seven (7) columns of information which depict a logical progression of information showing various prescriptions' costs, retail price, marginal profits and percentage of marginal profits within certain price ranges. By contrast, the report in QS/1 contains eleven (11) columns of information. There are four (4) columns of information which appear nowhere in the pc I report nor even in the pc I system. It is highly unlikely that the author or the sales analysis module of the pc I system would write a detailed set of programs and then simply copy seven of eleven columns from a single QS/1 report. The court finds that there is no substantial similarity between the

QS/1 report and the pc I report in the sales analysis portion of the two systems.

Narcotic and Controlled Drug Report

SDP has also complained about a certain report, referred to as the Narcotic and Controlled Drug Report which is printed by both the pc I and QS/1 systems.[3] SDP complains that columns of information contained in the reports generated by both systems are in substantially the same order. However, the columns generated by the pc I system are named differently from the columns on the report generated by the QS/1 system. Moreover, Max Gregory of SDP and Ken Hill both agreed that Canadian law requires the reporting of the information contained in the Narcotic and Controlled Drug Report.

As enhancements are suggested by end users or distributors of the various pharmacy computer systems, companies gradually change their computer systems. In fact, it is fair to say that enhancements are market driven. The court is not persuaded that the Narcotic and Control Drug Report being similar in the two systems in question is evidence of copying by SDP or pc I. Rather, from the explanation provided by both Gregory and Hill, it is clear that a Narcotic and Control Drug Report was required to service the Canadian market. Since the QS/1 system is sold in Canada and since the pc I system was written in

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[3] The parties were unable to stipulate exactly when the Narcotic and Controlled Drug Report was added to the pc I system. Because of the court's findings on this issue, the exact date on which this component was attached to the system need not be addressed.

Canada for distribution both in Canada and the United States, the mere fact that the reports contain similar columns of data is not persuasive evidence of copying.

Plaintiff has not shown substantial similarity with respect to this report. Accordingly, the court finds that there is no copying or infringement with respect to the Narcotic and Controlled Drug Report.

Patient Counseling Data

Shortly after SDP purchased the QS/1 Pharmacy System from G&H, it also purchased from G&H the rights to a list of drugs commonly used by pharmacists to fill prescriptions. This list contained certain drug interaction information. It also contained alpha characters and numbers that represent patient counseling messages which appear on labels printed by the QS/1 Pharmacy System once the drug list has been loaded into the computer system. These patient counseling messages are selected from a list of messages compiled by G&H. For each message there is an alphabetic letter or a number which serves as a code for that particular message. Therefore, where there is an indication or contra-indication for a particular drug which should be given in the form of a patient counseling message to a patient, the drug, on the drug list, has beside it a code for the appropriate message.

The indications and contra-indications for drugs are readily available in sources such as the *New England Journal of Medicine, The Physician's Desk Reference* and also informational inserts in the packages of drugs. While the

information is available to a researcher, it must be compiled and coded by someone with substantial knowledge of the drugs. When G&H first designed the drug list, it designed the format for the patient counseling messages. In this format G&H assigned the particular alpha or numeric codes to each message. SDP continued to use this coding format. The G/H Plus product likewise uses this coding format as does the pc I system.

Upon purchasing the rights to use the drug list from G&H, SDP contracted with the University of South Carolina Pharmacy Department to update and enhance that list. The University of South Carolina's Pharmacy School added many drugs to that list and designed a matrix for the enhanced list which would alert a pharmacist in the event the drug of one prescription interacted with the drug of another prescription for the same patient.

The University of South Carolina's Pharmacy School also added updated patient counseling messages by using the same coding format furnished to SDP by G&H. The initial cost to plaintiff for having this work done was approximately twenty seven thousand ($27,000.00) dollars. The value of the Patient Counseling Data to plaintiff's computer pharmacy system is substantial.

The Patient Counseling Data was made available by plaintiff to its licensed distributors and end-users on May 31, 1983, the date on which it was mailed. The court finds that the pc I drug file was not added to the pc I system until after the effective date of the settlement and thus this claim is not barred by the settlement agreement.

QS/1 has a drug list of some twelve thousand drugs, whereas pc I has no standard drug list. The various drug

lists for pc I presented at trial contain approximately 3,000 drugs each. The software of each of the three pharmacy systems (QS/1, pc I and G/H Plus) has been designed to recognize the alpha or numeric characters on a drug list when a drug list is loaded into the system. When a prescription is filled with a particular drug, each of the three systems will print a label with a patient counseling message according to the coding format.

Since pc I obtained the coding format from the G/H Plus product, SDP does not complain about the use of the coding format. Rather, SDP complains that pc I has a list of drugs which contains patient counseling codes that are substantially similar to the QS/1 list of drugs.

It was important that the pc I system include patient counseling capabilities in order to be competitive. Defendants intended to use the patient counseling data program of Medi-Span, a market competitor, as well as Medi-Span's interaction file. Defendants in fact purchased the interaction file. However, Medi-Span's patient counseling data program was not yet ready for marketing. Additionally, defendant would have had to invest a substantial amount of time and capital in the development of its own list.

Plaintiff's expert, Dr. Michael Dickson of the University of South Carolina Pharmacy School made an extensive comparison of the pc I drug list and the QS/1 drug list to determine the likelihood that plaintiff's Patient Counseling Data was copied by defendants. The following analysis summarizes his comparison:

Number	Explanation
2815	Total records in pc I
1485	pc I records with counseling codes exactly matching QS/1 codes
867	Additional records which would have matched exactly except for the fact pc I did not use the characters 1, U and Z as did QS/1, but rather left the position blank.
372	pc I records with no counseling code whatsoever.

Dr. Dickson accounted, in large measure, for the relatively few remaining unmatched records through a difference in package size, difference in strength of the active ingredient, and difference in dosage form. In addition, Dr. Dickson found that a significant number of common errors and anomalies pervade the drug list which he examined. For example, examination of the patient counseling codes for the drugs Dopar and Laradopa contain errors which cannot be satisfactorily explained. Both drug lists operated under a procedure whereby the patient counseling codes are alphabetically ordered. With regard to Dopar and Laradopa, however, there exists a transposition of the letters "C" and "G" resulting in an arrangement that is not entirely alphabetical. These two drugs in QS/1 list as follows:

Drug	Codes
Dopar 100 mg	AGCH
Dopar 250 mg	AGCH
Dopar 500 mg	AGCH
Larodopa 250 mg	AGCH
Larodopa 500 mg	AGCH

These five entries on the pc I drug list contain the same transposition of the letters "C" and "G." These five entries represent the only instances in either drug list where a pure alphabetical arrangement is not followed.

Another anomaly occurs in the use of the counseling code "P." Originally, QS/1 used this code to indicate "must interrupt therapy" meaning that the user should discontinue any therapy while using the drug. QS/1 later changed the definition for the letter "P" to "may cause dizziness." Pc I's definitional section continued to suggest that the code "P" meant "must interrupt therapy" (the *old* definition used by QS/1) but the pc I drug list uses the letter "P" on certain drugs where this counseling message would be inappropriate. For example, the "P" code is used in both QS/1 and pc I for the drug nitrate. A nitrate user is appropriately advised that the drug may cause dizziness under the QS/1 program, but pc I, using the old definition for "P" incorrectly, and perhaps dangerously, advises the user that he must interrupt ongoing therapy if he takes that particular drug.

A further anomaly occurs where the pc I file has counseling codes which are obviously inappropriate. In each case, the codes are correct for the *oral* dosage form of the drug as found in the QS/1 file. The code, however, was incorrectly placed on the *topical* dosage of the same drug in pc I. For example, both lists correctly use the "F" counseling note ("take with a full glass of water") for an oral dosage of achromycin. The pc I list, however, has the same code for a *topical* dosage of achromycin, an instruction clearly inapplicable for a medicine to be dropped in the user's eye.

Similarly, the codes for both systems are correct for the oral dosage of Celestone, but defendant's drug list contains an inappropriate code for the topical dosage of the same drug, advising the user that the topical application should be made "with [or] after food or milk". A person independently coding products from an information source (i.e., reference books) would be very unlikely to make this mistake, especially so consistently. It is likely, however, that an unknowledgeable person incorrectly copied the codes from the QS/1 file.

The inappropriate instructions found in the pc I list are as follows:

Drug	pc I	Counseling Notes	Dosage Form
Achromycin V 1%	00	FKLMNS	Ophthalmic Ointment
Achromycin V 1%	OS	FKLMNS	Ophthalmic Solution
Celestone Cream	15GM	CGJ	Topical
Celeston Cream	45GM	CGJ	Topical

In addition to the foregoing, there is another category of anomalies in the pc I list which suggest copying by an inexperienced typist. In large part, these errors can best be described as "alignment errors." That is to say, the code entered on the pc I list is identical to the code for the drug immediately preceding or immediately following the drug containing the incorrect code.[4]

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[4] Drugs on the pc I list containing this type of error include Dilantin W/PB, Empirin W/Codeine # 2 and # 3,

(Continued on following page)

The persuasiveness of the similarities, common errors, and anomalies recited above is heightened by the inability of the defendants to offer any credible explanation for the origin of their drug file.

In explaining how the drug file was composed, the defendants first stated, in answer to interrogatories, that

> . . . [i]n the early summer of 1983, James Smith . . . coded a drug file utilizing the G&H Limited drug file. This drug file has been used by pc I in the pc I Pharmacy System . . .

During James Smith's deposition of April 10, 1986, the following exchange took place:

Q. Did you personally code any of the drugs . . .

A. No.

Q. –with patient counseling messages.

A. No, I did not

Following Mr. Smith's deposition, Mr. Hill was deposed on June 5, 1986:

A. . . . A pharmacist, particularly one with Rod's (Ashbaugh's) knowledge of drugs, can sit down with that list and sit down at a computer system and go from one drug to the next and tie the letter code that corresponds to that counseling message to a drug . . .

Q. Okay. You're telling me that he (Ashbaugh) independently created it.

(Continued from previous page)

Furoxone Liquid & 100 mg Tablet, Novafed Capsule, Phenaphen Capsule, Phenergan VC W/Codeine, Povan 50 mg tablet, Quibron Products, and Ryna C Syrup.

A. That's correct.

Mr. Ashbaugh was deposed on August 29, 1986:

Q. Do you know where the patient counseling that is in the pc I System came from?

A. I have no idea, no.

* * *

Q. Okay . . . We have been informed, in Answers to Interrogatories, that you, among several others, in fact, coded in the patient counseling, and as I understand your testimony today, is that you did not, is that correct?

A. I did not.

Additionally, Hill's testimony about the number of drug codes he himself coded into the drug file has been inconsistent throughout this litigation. At various times, when asked about his participation, Hill responded that he coded "three to five" drugs, then "fifteen to twenty" drugs. He also responded to questions by saying "I would say it was less than two hundred" and, again later "the only ones I ever included were . . . those drugs used in a demonstration of the systems, which was Valium, Sumycin and maybe one or two others." Hill also testified at trial that he instructed temporary clerical help to code drugs of the same class in the same way as he had done.

Hill is thus unable to offer a cogent explanation for what he did and what others of the defendants did in developing the pc I Patient Counseling Data. Additionally, there was never an adequate explanation given to show how all the information was finally compiled and under whose direction the assembled information was entered into pc I.

The similarities, common errors and anomalies discussed above, coupled with defendants' inability to offer any credible, or even consistent, version of how the pc I drug list was developed, leads this court to find that the pc I drug list was copied from the QS/1 drug list. There is no consistency to the errors and anomalies which could be construed, even remotely, as a philosophical difference which might result from the independent creation of the codes.

In October of 1983, Couch saw the pc I drug list being demonstrated and was, in his words, "ninety percent certain" that the pc I patient counseling codes and messages had been copied from QS/1. This action was filed on July 16, 1985.

State Law Claims

In addition to copyright infringement, plaintiff sets out causes of action for misappropriation of trade secrets and the violation of the South Carolina Unfair Trade Practices Act, *S. C. Code Ann.* § 39-5-10 *et seq.* (Law. Co-op. 1976).

The allegations of the complaint fail to state a separate factual basis which could support a finding in plaintiff's favor on these claims. The damages claimed for the state law torts are the same as those claimed for the copyright infringement. Accordingly, these two state law claims are preempted under 17 U.S.C. § 301(a), as discussed more fully in the conclusions of law which follow.

Counterclaims

Defendants have counterclaimed for abuse of process, breach of the settlement agreement, tortious interference with contractual and business relationships and unfair trade practices.

The court finds that this action was brought in good faith, that the claims were colorable when brought, and that the action was not brought for an ulterior purpose.

The court also finds that there has been no breach of the settlement agreement by plaintiff. The fact that plaintiff's claims to presettlement copying were disposed of by way of summary judgment does not inevitably lead to a finding that the settlement agreement has been breached. The mere fact that the settlement agreement did not forever end the parties' dispute does not mean that either party breached the agreement. It must be remembered that plaintiff's complaint also alleged a breach of the settlement agreement, and alternatively sought to set the agreement aside on the ground of fraud. All parties have fully complied with the various duties required by the agreement. Accordingly, defendants' counterclaim for breach of the agreement is unsupported by the facts of this case.

Damages

Having found that there was copying of the QS/1 drug list, but not the QS/1 Pharmacy System itself the court must now address the question of damages. Plaintiff has conceded, and the evidence is conclusive, that plaintiff's copyright registrations were not made within

three months after defendant's first publications of pc I and the drug file.[5] Accordingly, statutory damages and attorney's fees cannot be awarded to plaintiff as a matter of law. 17 U.S.C.A. § 412 (West 1977).

With regard to actual damages and profits of the infringer, undisputed testimony at trial demonstrated that the pc I drug list was available at no additional charge to the purchaser. It was included in some, but not all, of the pc I systems sold or distributed by defendants. Plaintiff presented no testimony as to how many pc I drug lists were sold, distributed, or given away by pc I or any of the other defendants. More importantly, there was no evidence that the inclusion of the drug list in the pc I system caused more of the systems to be sold. In short, pc I's drug list was but a minor appendage to the system, available at no additional cost, which was included in some indeterminate number of pc I systems. Therefore, in the absence of any evidence as to the volume of sales which plaintiff would have obtained but for the infringement, or which defendant did obtain because of the infringement, the court is constrained to reject plaintiff's damage claim as being too speculative.

CONCLUSIONS OF LAW

This court has jurisdiction of the parties and of the subject matter of this action pursuant to 28 U.S.C. §§ 1332(a) and 1338(a) and pursuant to principles of pendent jurisdiction. Venue is proper before this court

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[5] The drug file copyright bears an effective date of April 4, 1985.

under 28 U.S.C. § 1391(b), in that the controversy arose within this judicial district.

Plaintiff is the owner of all right, title and interest in and to the QS/1 Pharmacy System, including all copyrights therefor.

Plaintiff is the owner of copyright registration TXu 189-270, which is the entire work of each separate element of the collection of the QS/1 Pharmacy System and of supplemental copyright registration TXu 197-301. The former registration is effective as of April 4, 1985 and the latter is effective as of June 20, 1985.

Plaintiff is the owner of copyright registration TXu 189-274, which is the textual material as appears on the various screens of the QS/1 Pharmacy System, effective April 17, 1985.

Plaintiff is the owner of copyright registration TXu 189-272 on patient counseling data of the QS/1 Pharmacy System effective April 4, 1985.

All of the foregoing copyrights are valid.

Copyright Infringement

"As the term 'copyright' suggests, it is the act of copying which is essential to, and constitutes the very essence of all copyright infringement." 2 M. Nimmer, *Nimmer on Copyright* § 8.02[A].

Section 106 of the Copyright Act provides that the owner of the copyright has the exclusive right, *inter alia*, to reproduce the copyrighted work, to prepare derivative works based on the copyrighted work and to distribute

copies of the copyrighted work by sale or other transfer of ownership or by rental, lease or lending.

To prevail in a copyright infringement action, a party must demonstrate ownership of the copyright as well as impermissible copying. *Ferguson v. National Broadcasting Co., Inc.*, 584 F.2d 111 (5th Cir. 1978). Infringement is quickly established where there is evidence of actual copying by the defendant. However, since direct evidence of copying is seldom available, infringement usually must be proven through circumstantial evidence.

In this action, there being no direct evidence of copying as to the copyright infringement claims of plaintiff, copying must "be proved inferentially by showing that the defendants had access to the allegedly infringed copyrighted work and that the allegedly infringing work is substantially similar to the copyrighted work." *Whelan Associates, Inc. v. Jaslow Dental Laboratory, Inc.*, 797 F.2d 1222, 1232 (3d Cir. 1986), *cert. denied*, 107 S. Ct. 877 (1987). *Accord, M. Kramer Manufacturing Co. v. Andrews*, 783 F.2d 421, 455 (4th Cir. 1986).

In *Whelan*, the court held that the scope of copyright protection for computer programs extends beyond the program's literal source or object code to include the programs structure, sequence and organization. The *Whelan* court determined a way to distinguish idea from expression in software cases: The purpose or function of the program is the idea, and everything not necessary to that purpose or function is the expression of the idea. In other words, if there are different ways to create a program to accomplish a desired purpose or function, then the particular way chosen by the programmer to achieve

that end is not necessary to the computer's function and is, therefore, expression.

The Fourth Circuit, in *Kramer*, likewise held that since there are virtually unlimited numbers of instruction sequences that would enable a programmer to construct a program with the same function as another, courts, in copyright cases involving computer programs, are normally concerned with copyrightable "expression" rather than "idea" outside of copyright protection. *Kramer*, 783 F.2d at 436, paraphrasing "Computer Copyright Law: An Emerging Form of Protection for Object Code Software After *Apple v. Franklin*," 5 Computer L.J. 233, 251 (1984).

The Fifth Circuit in *Plains Cotton Cooperative Assn. v. Goodpasture Computer Service*, 807 F.2d 1256, 1262 (5th Cir. 1987), cert. denied, 108 S. Ct. 80, declined to follow *Whelan*. However, that case involved a review of a denial of a motion for a preliminary injunction and the record was not sufficiently developed. In addition, marketing factors may have determined the sequence and organization of that plaintiff's program and, hence, such sequence and organization may be unprotectable ideas. This court, however, follows the reasoning of the *Whelan* and *Kramer* cases, and recognizes there are numerous ways to create a program to accomplish the desired purposes of a pharmacy system. Therefore, the structure, sequence and organization of the QS/1 program constitutes "expression" and is fully protectable under the copyright laws.

Defendants have had access to the QS/1 Pharmacy System and, since May 31, 1983, have produced a Nursing Home Module, a Sales Analysis Program, a Narcotics and Controlled Drug Report and Patient Counseling

Data. Plaintiff acknowledges that pc I is in many respects dissimilar from QS/1, but this fact does not indicate non-infringement by defendants. *See Whelan*, 797 F.2d at 1245. "No plagiarist can excuse the wrong by showing how much of his work he did not pirate" and is different from plaintiff's. *Sheldon v. Metro Goldwyn Pictures Corp.*, 81 F.2d 49, 55 (2d Cir.) *cert. denied*, 298 U.S. 669 (1936).

Except for the QS/1 drug file, discussed below, and the nursing home component, plaintiff's evidence was insufficient to support a finding of substantial similarity which could give rise to an inference of copying of the QS/1 system.

Access and substantial similarity, however, are not conclusive evidence of copying. Defendants can rebut the inference of copying raised by proof of access and substantial similarity by demonstrating coincidence, independent creation, or common source. *Benson v. Coca-Cola Co.*, 795 F.2d 973 (llth Cir. 1986).

Since the pc I system is based upon G&H Plus and since QS/1 and G/H Plus have common origins, similarities between pc I and QS/1 are naturally to be expected. Similarities which otherwise might be considered conspicuous evidence of copying become rather insignificant. Moreover, the May 31, 1983 release of all claims necessarily released claims as to functional or "structural similarities" in the defendants' pc I Pharmacy System as of May 31, 1983. Plaintiff's claims concerning alleged infringement of the logic and flow of QS/1 are, therefore, without merit.

In addition to producing evidence of common origins between the systems, defendants presented evidence of

common origin particularly regarding the nursing home module. While significant similarities exist between the pc I and the QS/1 nursing home modules, the fact remains that defendant Hill made valuable contributions to both systems. Hill not only investigated the market to determine the particular requirements of servicing a nursing home but also compiled information on the alternative systems available to pharmacists serving nursing homes. Hill shared his findings and resources with SDP and worked with SDP's programmers in the development of QS/1's nursing home programs. Later, when Hill, through pc I Corp., assisted the pc I programmers develop pc I's nursing home module, he undoubtedly brought to the project the same information, experience, and know how he had furnished to SDP. Despite extensive effort, the court is unable to find support, either in law or fact, for plaintiff's position that Hill's actions in this regard infringed plaintiff's copyrights.

Furthermore, no obligation, legal or contractual, compelled Hill to refrain from using his own ideas and the information he had compiled to design the pc I nursing home module. The court concludes that the relationship of the defendants as distributors of QS/1 was set out by the terms of the license agreements which are in evidence and that as independent distributors, they were not required to give information for ideas or enhancements exclusively to SDP. Specifically, two of the defendants, King and Ashbaugh, as well as other distributors of QS/1 were permitted by SDP to sell competing systems while they were QS/1 distributors. If there were some requirement at law that such distributors would have to furnish exclusively to SDP information for enhancements of the

computer systems they were selling which they derived from the field, then, on the same theory, they would be in breach of some duty to the other company whose product they distributed. The court can find no legal or factual basis from which to conclude that SDP was exclusively entitled to features or ideas for enhancements which the distributors developed themselves or learned from others in the marketplace. Rather, the court concludes that there is no basis for SDP to maintain that once a distributor furnishes information to enhance the QS/1 system that it becomes the exclusive property of SDP to the exclusion of the distributors themselves and all others.

As to the alleged infringement of Patient Counseling Data in the separately copyrighted SDP drug file, the court has found that substantial similarity does exist between the two systems. The courts have consistently regarded the existence of common errors in two similar works as the strongest evidence of copying. *Kramer*, 783 F.2d at 446; 3 M. Nimmer, *Nimmer on Copyright* § 13.03[C], at 13-44 (1988). In the present case, several hundreds of patient counseling codes are exactly identical including those codes for the drugs Dopar and Larodopa which represent the only five patient counseling codes which are not in alphabetical order. Such expected "glitches" in an otherwise homogeneous system have likewise been regarded by the courts as evidence of copying.

Of especial relevance to the present case is the Second Circuit decision of *Eckes v. Card Prices Update*, 736 F.2d 859 (2d Cir. 1984). In that case, plaintiffs had published a baseball card price guide listing some 18,000 baseball cards including a list of 5,000 "premium" cards.

Defendants' infringing work included a list of 5,000 premium cards substantially the same as plaintiffs' list. Both works contained a 1933 "Delong" series. Although throughout their guide plaintiffs often listed players by both first and last name, in the "Delong" series they listed all of the players by their last name with only two exceptions – "Lou Gehrig" and "W. Terry." Likewise, defendants' infringing work listed all of the players in the "Delong" series by last name with the exception of "Lou Gehrig" and "W. Terry." The court found this common anomaly to be an example of "indisputable copying." *Eckes*, 736 F.2d at 864.

In the present case, the chance that defendants would coincidentally assign to hundreds of drugs the identical patient counseling codes previously assigned by plaintiff to those same drugs is about as likely as the defendants in *Eckes* listing the same 5,000 premium cards as plaintiffs in that case. Likewise, the chance that the defendants would coincidentally list the same five codes in nonalphabetic order as those five listed in nonalphabetic order by plaintiff is about as likely as defendants in *Eckes* making the same exceptions to a "last name only" list as those made by plaintiffs in that case.

While the above examples clearly indicate that defendants copied plaintiff's patient counseling codes, other examples of copying are to be found throughout defendants' drug list. Some codes which represent the topical form of an oral drug represented above or below it on a drug list include the symbol for "Take with Water" which should be found only in the code for its oral counterpart. This anomaly indicates that the codes were manually copied and that the copier was not familiar with the code

symbols or with the drugs. Also, defendants included the code symbol "P", originally designated by plaintiff for one purpose and later changed to indicate "Must interrupt Therapy." Defendants maintained "P" where originally copied, giving the inappropriate message of "Must Interrupt Therapy" for certain drugs. The presence of an arbitrary code or symbol which can only be explained by copying has been found to be evidence of "slavish imitation." *Joshua Meier Co. v. Albany Novelty Mfg. Co.*, 236 F.2d 144, 146 (2nd Cir. 1956). It is well established that the existence of brief phrases contained in two separate works which are so idiosyncratic as to preclude coincidence is very strong evidence of copying. *Heim v. Universal Pictures Co.*, 154 F.2d 480, 488 (2nd Cir. 1946).

Estoppel

Defendants contend that the twenty-two month delay between Couch's "ninety percent certain" determination that copying of the drug file had occurred and the institution of this action present a "classic case of estoppel."

In order for estoppel to operate as a defense, four elements must be present:

(1) the party to be estopped must know the facts of the defendant's infringing conduct;

(2) he must intend that his conduct shall be acted on or must so act that the party asserting the estoppel has a right to believe that it is so intended;

(3) the defendant must be ignorant of the true facts, and

(4) he must rely on the plaintiff's conduct to his injury.

Hampton v. Paramount Pictures Corp., 279 F.2d 100 (9th Cir. 1960).

Here, it is clear beyond peradventure that elements two and three have not been shown. There was no evidence that plaintiff intended that its inaction be acted upon by the defendant. Similarly, there was no showing that the defendants were ignorant of the true facts regarding their own drug file. Accordingly, the defense of estoppel has not been made out.

Damages

In a copyright infringement action under the 1976 Act, a plaintiff may recover actual damages, infringer's profits, or statutory "in lieu" damages. 17 U.S.C.A. § 504 (West 1977). Unlike its predecessor, the 1909 Act, the new act provides that there shall be no duplication of damages. Section 504(a) provides that plaintiff is entitled to actual damages and profits that are "additional" to those damages. The third category, statutory damages, are available only if plaintiff has met certain registration requirements, and if plaintiff has elected, prior to judgment, to seek an award of statutory damages. Here plaintiff has stipulated on the record that it does not seek to recover statutory damages. Moreover, plaintiff has conceded, and the evidence is conclusive that plaintiff's copyright registrations were not made within three months after defendants' first publications of the pc I product and patient counseling data. Accordingly, statutory damages and attorney's fees

cannot be awarded to plaintiff as a matter of law, assuming, *arguendo*, any establishment of infringement. 17 U.S.C.A. § 412 (West 1977); *Evans Newton Inc. v. Chicago Systems Software*, 793 F.2d 889, 896-97 (7th Cir.), *cert. denied*, 107 S.Ct. 434 (1986); *Whelan Associates, Inc. v. Jaslow Dental Laboratory, Inc.*, 609 F. Supp. 1325, 1330-31 (E.D. Pa. 1985), *aff'd*, 797 F.2d 1222 (3d Cir. 1986), *cert. denied*, 107 S.Ct. 877 (1987); *Johnson v. University of Virginia*, 606 F. Supp. 321, 324-25 (D.Va. 1985).

Likewise, plaintiff did not attempt to recover defendants' profits. Instead, plaintiff seeks to recover actual damages in the form of its lost profits. Plaintiff's testimony at trial focused entirely upon the total sales of the defendants, claiming that plaintiff would have made at least 90-95% of those sales. Simply stated, it is the position of the plaintiff that practically all of defendants' increased sales due to the infringement would have been sales by the plaintiff but for the infringement.

In copyright cases, as in all cases, the court may not award speculative damages. *Baldwin Cooke Co. v. Keith Clark, Inc.*, 420 F. Supp. 404 (N.D. Ill. 1976). "Although uncertainty as to the amount of damages will not preclude recovery, uncertainty as to the fact of damages may." *Frank Music Corp. v. Metro-Goldwyn-Mayer, Inc.*, 772 F.2d 505, 513 (9th Cir. 1985), citing *Universal Pictures Co. v. Harold Lloyd Corp.*, 162 F.2d 354, 369; and 3 M. Nimmer, *Nimmer on Copyright* § 14.02 at 14-8 to 14-9 (1985).

Plaintiff has failed to meet its burden of proof as to damages. In a copyright infringement case, it is plaintiff's burden to show *what number of sales* (or, even more specifically, resulting "gross revenue" therefrom, 17 U.S.C. §

504(b)) *were made of products incorporating the infringing components. RSO Records, Inc. v. Peri,* 596 F. Supp. 849, 860-62 (S.D.N.Y. 1984) . Defendants' evidence was uncontroverted. A drug file diskette was not always provided with a pc I Pharmacy System. The plaintiff simply failed to elicit any evidence as to *how frequently* the drug file was in fact included with sales of the pc I system. Consequently, no award of damages due to allegedly lost QS/1 sales by SDP, ostensibly resulting from the indeterminate, sporadic inclusion of drug file diskettes with pc I sales, can be made. While the court is mindful of the fact that in infringement cases the risk of uncertainty as to damages is upon the alleged infringer, SDP has completely failed to provide this court with a rational basis upon which to conclude that any damages have, in fact, been sustained.

Even had the court determined that defendants had engaged in copying of the other components of plaintiff's QS/1 system, the sole basis upon which plaintiff claims damages is unfounded. Plaintiff would not necessarily have made all of the sales which the defendants made even if the court were to assume, *arguendo,* that there had been copyright infringement of the entire system. Of particular significance is the disparity between the prices of the two systems. As the court noted in *Stevens Linen Associates, Inc. v. Mastercraft Corp.,* 656 F.2d 11, 14-15 (2d Cir. 1981), the difference in price between the infringed and infringing products militates against a finding of damages based upon the assumption that plaintiff would have sold the entire amount of products sold by the defendants. Additionally, undisputed testimony revealed

that defendants targeted chain stores. By so doing, defendants were tapping new markets into which plaintiff had not ventured.

More importantly, the pc I product was sold on an IBM personal computer whereas in 1983 and a part of 1984, the QS/1 product was not. Both plaintiff's and defendant's witnesses agree that the marketplace is price driven and that hardware is a significant factor in the pricing of the system. Further, the IBM personal computer is admittedly the hardware of choice. Since QS/1 did not run on a personal computer in 1983 and 1984, most of plaintiff's "lost sales" would have occurred whether defendants pirated plaintiff's system or not. *See, e.g., Harper & Row v. Nation Enterprises*, 471 U.S. 539, 567 (1985). For these reasons, the court cannot conclude that SDP would have made all or any significant portion of the sales that defendants made for the relevant periods of time.

In addition to its claim for actual damages, plaintiff seeks an award of punitive damages. While some courts have awarded punitive damages in common law copyright infringement cases, such damages are not recoverable as a matter of right. In a statutory copyright infringement action, however, it is clear that punitive damages should not be awarded. 3 M. Nimmer, *Nimmer on Copyright* § 14.02[B], at 14-19 and cases cited thereon. In any event, the conduct of the defendants, either individually or collectively, falls far short of being willful, wanton, or malicious. Consequently, plaintiff's request for punitive damages should be denied.

Accordingly, as to the Nursing Home, Sales Analysis, Narcotic and Controlled Drug Report, as well as the

structure and flow of the QS/1 system itself, the court concludes that there has been no copyright infringement. Alternatively, even if a copyright infringement of one or more of these items had been shown, the court is not persuaded that any lost sales of programs compatible with personal computers was due to the infringement. With regard to the separately registered QS/1 drug file, plaintiff has shown copyright infringement, but has failed to meet its burden of proof as to damages. Accordingly, the only relief to which plaintiff would be entitled is an injunction against further infringement.

State Law Claims

As to the two state-law claims left pending after the court's summary judgment ruling and plaintiff's abandonment announcement at the start of trial, the court concludes these claims are preempted under 17 U.S.C. § 301(a). Although Counts XI and XII are denominated unfair trade practices and misappropriation claims, respectively, SDP specifically refers to the copyrighted nature of the allegedly misused or misappropriated material in each instance. SDP further advanced no separate theory of harm or damages predicated on those counts at trial. Accordingly, since the basis of plaintiff's two state-law claims is in fact the alleged taking, misuse, or unauthorized publication or sale of material which, as plaintiff again specifically alleges, is the subject of copyright law, then any state law which might otherwise have been pertinent is preempted.

This conclusion is squarely in accord with the precise holding in *Videotronics, Inc. v. Bend Electronics*, 564 F.

Supp. 1471 (D.Nev. 1983). In that case, quite by contrast to the evidence herein, the undisputed evidence was that defendant had "copied plaintiff's electronic video poker game." *Id.* at 1473. Thus, a "classic case for application of the law of misappropriation" was presented, aside from the preemption question. *Id.* at 1476. Nonetheless, the clearly controlling rule of law was that "a property which is subject to protection under federal . . . copyright law cannot also obtain the benefit of protection under either state unfair competition or misappropriation law." *Id.* Again, the rule of preemption is even more clearly applicable in this action because plaintiff herein, in contrast to *Videotronics, has* "sought protection under the Copyright Act." *Id.* at 1477. Therefore, since plaintiff's property interest in the computer programs is protected by the Copyright Act, relief under the state doctrines of misappropriation and unfair trade practices cannot be obtained here.

Although not as closely on point as *Videotronics*, several other recent cases further support this court's holding of preemption in this action. *See Del Madera Properties v. Rhodes and Gardner, Inc.*, 820 F.2d 973, 976-77 (9th Cir. 1987); *Motown Record Corp. v. George A. Hormel & Co.*, 657 F. Supp. 1236 (C.D. Cal. 1987); *Universal City Studios, Inc. v. T-Shirt Gallery, Ltd.*, 634 F. Supp. 1468, 1474-76 (S.D.N.Y. 1986). Counts XI and XII of plaintiff's complaint are therefore preempted.

Counterclaims

In South Carolina, the tort of abuse of process consists of two elements:

(1) an ulterior purpose; and

(2) a wilful act in the use of process not proper in the regular conduct of the proceedings.[6]

Mere commencement of a civil action does not amount to abuse of process. Here, there has been no credible evidence that plaintiff brought this action for an ulterior purpose, and accordingly, the counterclaim for abuse of process is not viable.

Similarly, there is no merit to defendants' tortious interference claims. South Carolina does not recognize the torts of tortious interference with business relationships, *Columbia Management Corp. v. Resort Properties, Inc. of Beaufort*, 279 S.C. 370, 307 S.E.2d 228 (1983) or tortious interference with prospective advantage, *Smith v. Holt, Rinehart and Winston, Inc.*, 270 S.C. 446, 242 S.E.2d 548 (1978). With regard to the tort of tortious interference with contractual relations, which is recognized in South Carolina, *Todd v. South Carolina Farm Bureau Mutual Insurance Co.*, 287 S.C. 190, 336 S.E.2d 472 (1985), the plaintiff must establish (1) the existence of the contract; (2) the wrongdoer's knowledge of the contract; (3) the intentional procurement of its breach; (4) the absence of justification; and (5) resulting damages. *DeBerry v. McCain*, 275 S.C. 569, 574, 274 S.E.2d 293, 296 (1981).

Here, there has been no showing of a breach of any contract entered by the defendants, much less a showing of intentional procurement of a breach by plaintiff. Consequently, this counterclaim must also fail.

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[6] *Huggins v. Winn-Dixie Greenville, Inc.*, 249 S.C. 206, 153 S.E.2d 693 (1967).

Defendants' counterclaim for unfair trade practices is similarly without merit. Having determined that plaintiff did not bring this action for ulterior purposes, the court is constrained to hold that plaintiff's actions in bringing this suit and in litigating it were not for the purpose of hindering competition. Consequently, this counterclaim must fail.

Injunctive Relief

The Copyright Act expressly provides for injunctive relief. Such relief must be structured in a way "reasonable to prevent or restrain infringement." 17 U.S.C.A. § 502(a) (West 1977).

Inasmuch as the court has found that copying did occur with regard to the QS/1 drug file, but not with regard to the remainder of the QS/1 system itself, injunctive relief in this case must be narrowly tailored to restrain infringement of the copyright found to have been violated. The court's task in this regard is made less difficult by reason of the fact that the drug file is, as noted above, a separate component of the pc I system, which is easily removed therefrom. It follows, therefore, that the injunction issued should simply prohibit the defendants from utilizing the Q/S 1 drug file in any of its systems sold in the future.

Judgment

For the foregoing reasons, it is hereby ORDERED as follows:

1. Judgment shall be entered in favor of all defendants as to Counts I and II of the complaint;

2. With regard to Count III, judgment shall be entered in favor of all defendants, the plaintiff having proved the copying alleged in this count, but having failed to meet its burden of proof as to any damages arising from the copying, *provided however*, that all defendants shall be subject to the permanent injunction set forth in paragraph 6 below.

3. Counts XI and XII of plaintiff's complaint are dismissed with prejudice as preempted.

4. All other counts of plaintiff's complaint were either abandoned or earlier dismissed with prejudice in this cause, and judgment is therefore rendered for defendants as to all remaining counts of plaintiff's complaint.

5. Judgment shall be entered in favor of the plaintiff as to all counts of the counterclaim.

6. All defendants and all persons in privity with defendants or acting on their behalf or in concert with them, are hereby enjoined from producing, advertising or offering for sale or lease, marketing, leasing, selling, distributing or otherwise dealing in or disposing of any copies of the pc/1 or pc I drug file, and are further directed to deliver up to the plaintiff all exact or substantial copies of the pc I drug file now in their possession.

7. Each party to this litigation shall bear its own attorneys' fees and costs.

IT IS SO ORDERED.

/s/ Joe F. Anderson, Jr.
Joe F. Anderson, Jr.
United States District Judge

Greenville, South Carolina

August 31, 1988

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
SPARTANBURG DIVISION

J M Smith Corporation, d/b/a Smith Data Processing, Plaintiff, vs. pc I Corp., Hill Pharmacy Group, Inc., Kenneth A. Hill, W. K. Enterprises, Inc., Wes King, Richie S. Lynn, d/b/a Rich-2 Pharmacy Consulting Services, Professional Systems, S.E., Inc., A. Rodney Ashbaugh, and Dr. T. C. Smith Company, Defendants.	C/A No. 7-85-1926-17 ORDER (Filed Aug. 7, 1987

This matter is before the court upon cross motions for summary judgment. Plaintiff has brought this action under the Copyright Act of 1976, 17 U.S.C. § 101, *et seq.* The complaint also alleges causes of action under various state law claims, as well as the Racketeer Influenced and Corrupt Organizations Act (RICO) 18 U.S.C. § 1961, *et seq.*

Plaintiff, J M Smith Corporation, d/b/a Smith Data Processing ("SDP") has sued pc I Corp. ("pc I") and the other defendants herein claiming the defendants have infringed on SDP's copyrighted pharmacy computer system. SDP claims that pc I's pharmacy system contains proprietary and confidential information and copyrighted

matter which was taken from SDP's pharmacy system, known as the "QS/1 Pharmacy System".

The parties have conducted extensive discovery and filed detailed memoranda and supporting authorities with this court. Extensive oral argument was conducted on July 15, 1987. For the reasons set forth below, both motions for summary judgment are denied. However, pursuant to Rule 56(d) the court has ascertained certain material facts that exist without substantial controversy, and these facts shall be deemed established in this litigation.

Rule 56(d) provides as follows:

> If on motion [for summary judgment] judgment is not rendered upon the whole case or for all the relief asked and a trial is necessary, the court at the hearing of the motion, by examining the pleadings and the evidence before it and by interrogating counsel, shall if practicable ascertain what material facts exist without substantial controversy and what material facts are actually and in good faith controverted. It shall thereupon make an order specifying the facts that appear without substantial controversy, including the extent to which the amount of damages or other relief is not in controversy, and directing such further proceedings in the action as are just. Upon the trial of the action, the facts so specified shall be deemed established, and the trial shall be conducted accordingly.

Plaintiff began as a wholesale pharmaceutical business in the 1940's. In 1977, plaintiff contracted with a partnership known as G & H Limited for the purpose of converting a computer program previously developed by G & H into a program compatible with and run on an

IBM Series 1 Computer. The program was to be prepared by SDP, but would be the exclusive property of G & H. The system developed under this arrangement has gone by various names at various times, although for purposes of this order, the system is known as the QS/1 Pharmacy System.

After development of this system, SDP, by license from G & H, sold this system in an assigned territory of the United States. Several of the various sales distributors for the QS/1 system are individual defendants in this case.

On June 22, 1981, G & H and SDP entered an agreement by which the existing QS/1 product was sold to SDP. Prior to the sale, the principals of G & H had begun to develop another pharmacy system, also known by various names, but, for purpose of this order, referred to as the G/H Plus Pharmacy System. There is no mention of the G/H Plus product in the June 22, 1981 sales agreement.

Following the June 22, 1981 agreement, SDP and G & H entered an additional written agreement, dated June 1, 1982. The purpose of that agreement was to permit SDP a non-exclusive right to use a data file, known as an "interaction matrix". This data file is not an integral part of the QS/1 system but was simply a drug data file which was sold to end users of the QS/1 system to be used in conjunction with it. This drug interaction file is used by pharmacists to notify them of potential problems when they are filling a prescription. By the 1982 agreement, G & H sold SDP the right to utilize the drug interaction and patient counseling codes in this drug file. SDP thereafter

employed the University of South Carolina to enhance the file and make it more complete.

After SDP bought the ownership rights to QS/1, most of the distributors elected to continue to sell the QS/1 product, and did so as independent distributors for SDP.

It soon became apparent that a lower cost product was needed to meet competition in the market place. The advent of the IBM personal computer at about this time provided added incentive for a pharmacy system which could be run on a micro-computer.

Seeking to capitalize upon the trend to smaller computers, Mark Lyle and Barry Guld, former employees of G & H, entered into an agreement with G & H for an exchange of technology relating to the G/H Plus product. The new system developed was compatible with an IBM personal computer. Thereafter, one of the defendants, Ken Hill, was persuaded to market this new pharmacy system. Hill formed a Texas corporation, pc I Corp., one of the defendants herein. This new corporation purchased all rights to the new pharmacy system from Lyle and Guld, and their corporation, Zadall.

Shortly thereafter, in the spring of 1983, this new system, then known as pc/1, was being demonstrated at a meeting of the American Pharmaceutical Association. Various representatives of SDP, upon viewing the new system, concluded that the system was substantially similar to the QS/1 product SDP had purchased from G & H.

SDP instructed its legal counsel to send a demand letter to Ken Hill and pc I Corp. The demand, in part, alleges copyright infringement and misappropriation of

confidential information. Upon receipt of the demand letter, Ken Hill and pc I, through their counsel, sent a responsive letter to SDP on May 12, 1983. The matters in dispute were set out in SDP's demand letter. It was alleged that Hill and pc I Corp. were infringing upon a trademark belonging to SDP, were infringing on SDP's copyright, and had misappropriated confidential information belonging to SDP by incorporating certain enhancements of SDP's pharmacy system into the pc/1 Pharmacy System. The demand letter requested that Hill and the defendants recall all of the pc/1 Pharmacy Systems and "remove all confidential, proprietary and/or copyrighted information therefrom."

In response to these demands, a settlement conference was held in Ft. Worth, Texas in May, 1983. During the settlement negotiations, Hill told the SDP representatives that he had not misappropriated SDP's confidential information and had not copied the QS/1 Pharmacy System. At the settlement conference, certain terms of a compromise were generally discussed. Thereafter several drafts of a settlement agreement were exchanged.

These negotiations culminated in a settlement agreement "entered into as of" May 31, 1983. Under the settlement agreement, SDP released pc I, Hill, and their agents, employees and servants from "any and all past and present claims [SDP] may have against Hill Pharmacy and/or pc/1 Professional relating from their individual or collective activities relative to the pc/1 pharmacy system." Additional provisions of the settlement agreement required SDP to assign in blank its stock in U.D.A., Inc., a corporation established by the parties for the purpose of

distributing certain IBM products. The settlement agreement also required that various defendants return QS/1 materials to SDP and required the cancellation of territorial agreements between various distributors and SDP. Defendants also agreed to change their trademark from "pc/1" to "pc I".

In the ensuing months, the parties performed basically all of the requirements called for under the settlement agreement. The final step occurred on January 17, 1984, when SDP forwarded, through its legal counsel, the shares in U.D.A. which SDP had agreed to transfer under the settlement agreement. The cover letter accompanying this stock indicated that both sides to the agreement had "concluded the various tasks" to be performed under the agreement and indicated that the matter was closed.

Sometime shortly after the settlement agreement was entered, SDP decided to convert its QS/1 Pharmacy System to make it compatible with an IBM personal computer. In July of 1985, approximately two years after the settlement agreement was entered, this litigation was instituted. In its complaint, SDP contends that "the pc/1 Pharmacy System includes computer programs which contain the organizational and structural expressions embodied in the SDP copyrighted computer programs which were willfully and wantonly copied therefrom." Additional causes of actions stem from this same basic contention.

Plaintiff has moved for summary judgment on Count I, which alleges that the copyrighted QS/1 computer program was infringed, and Count III, which alleges that

the copyright on the Drug Interaction and Patient Counseling Code has been infringed. The defendants have moved for summary judgment by raising the settlement agreement as a complete bar to all causes of action.

For the reasons set forth below, the plaintiff's motions for summary judgment on Count I and Count III are denied. Pursuant to Rule 56(d), however, the court does find that the following material facts exist without substantial controversy:

(1) SDP is the owner of all right, title and interest in and to the QS/1 Pharmacy System including all copyright therefor; and

(2) SDP is the owner of copyright registration TXu 189-270 and supplemental copyright registration TXu 197-301; and

(3) Said copyrights are valid.

For the reasons set forth below, the defendants' motion for summary judgment is denied. However, pursuant to Rule 56(d), the court finds that the following material facts exist without substantial controversy and, accordingly, upon the trial of this action, the facts so specified shall be deemed established, and the trial shall be conducted accordingly:

(4) The settlement agreement dated May 31, 1983, bars any claim for copyright infringement which occurred prior to the date of the settlement agreement; and

(5) Any act or acts of infringement occurring after May 31, 1983, including specifically any acts of infringement relating to the Drug Interaction and Patient Counseling Code and any infringement occurring after May 31,

1983 relating to any enhancements to the QS/1 Pharmacy System, are actionable.

With regard to plaintiff's motions for summary judgment, the court has carefully considered the authorities cited by plaintiff and has examined the rather substantial affidavits and depositions submitted in connection with the motion. Rule 56(c) provides that summary judgment shall be granted when the affidavits, pleadings, and other documents show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. The court is not prepared to say at this time that there is no genuine issue as to any material fact on Counts I and III. For this reason, the plaintiff's motions for summary judgment or these counts are denied.

A resolution of the defendants' motion turns on the proper interpretation of the settlement agreement entered in May of 1983. The defendants interpret the settlement agreement as an extinguishment of all of SDP's claims in this case. Plaintiff, on the other hand contends that the agreement is an executory accord, the terms of which have not been complied with by the defendants. Even if the defendants are able to prove they have fully performed their obligations under the agreement, plaintiff maintains that the settlement agreement is not a bar to this action because no license for the *future* was granted to any of the defendants for the use of SDP's confidential and proprietary information or for infringements of SDP's copyrights. In other words, plaintiff argues that the settlement agreement forgave any theft of SDP's confidential and proprietary materials which had occurred, as well as the use and infringements, up to the time of the

settlement agreement, but not any future such misappropriation, use or infringement.

After carefully considering the excellent memoranda and supporting authorities submitted by both sides, hearing over four hours of oral argument on July 15, 1987, and conducting a telephonic conference call on July 27, 1987, the court has concluded that the misappropriation which plaintiff claims in this action is, in part, the same misappropriation alleged by the plaintiff prior to the settlement agreement. Therefore, the settlement agreement bars any claim of misappropriation which occurred prior to the date of the settlement agreement.

In deposition, James Matthews Smith, Jr., former Chairman of the Board and one of SDP's designated corporate representatives pursuant to Rule 30(b)(6), testified that the claim sued upon in this case is basically the same claim made by the plaintiff prior to the settlement agreement. This contention is buttressed by the demand letter submitted by plaintiff's counsel in May of 1983, wherein SDP alleged:

> You have infringed our client's copyright by including significant portions of its program in your pc/1 Pharmacy System. It is therefore demanded that you immediately recall all of the pc/1 Pharmacy Systems and remove all of our client's confidential, proprietary and/or copyrighted information therefrom.

After subsequent negotiations, during which the defendants denied any misappropriation, the settlement agreement was executed. It provides, in pertinent part, that SDP releases

> Hill Pharmacy and pc/1 Professional, and their agents, employees, and servants from any and all past and present claims it may have against Hill Pharmacy and/or pc/1 Professional relating from their individual or collective activities relative to the pc/1 pharmacy system.

By arguing that the settlement agreement released past and present claims but did not license future activity, plaintiff seeks to read into the agreement a concession that the pc/1 system would no longer be marketed after the settlement. However, paragraph one of the settlement agreement provided that pc/1 Professional agreed to

> immediately change its tradename and trademark(s) to delete pc/1 therefrom and to use pc I in lieu thereof; to designate its computer system as "pc I Professional System", and not a "pc I Pharmacy System"; and to use as its logo, pc I with a rose in a horizontal disposition beneath same, all within an encircling, colored border; it being understood, not withstanding anything to the contrary herein, that pc/1 Professional shall have the right to use the trademark pc I.

The foregoing language makes it clear that the parties to the settlement agreement contemplated that the defendants would continue using the system, but under a different trademark. Had the parties, in fact, agreed that the pc I system would no longer be marketed after the settlement, language to that effect would have been included in the settlement agreement.

Glen Hammett, the President of SDP and one of its designated corporate representatives, also stated in his deposition that at the time of the settlement agreement, he knew that pc I would continue to sell the pc I Pharmacy System. Specifically, he admitted:

Q. All right sir. Did you understand after the Settlement Agreement that they were selling the pc I Pharmacy System?

A. Yes.

Q. You knew at the time of the Settlement Agreement that they would continue to sell the pc I Pharmacy System, did you not?

A. I assumed that they would, yes sir.

In short, the events leading up to the execution of the May 31, 1983 agreement appear to be those of a typical settlement situation One party makes demands; the other party denies those demands; the parties enter into settlement negotiations culminating in a settlement agreement wherein the parties make concessions to each other and execute mutual releases.

Defendants claim the actual effective date of the agreement is in August of 1983. However, paragraph 8 of the agreement clearly states that "[t]his agreement represents the entire understanding between the parties." Accordingly, the court is unwilling to go behind the document for a determination of the effective date. The effective date of the agreement therefore, is established to be May 31, 1983.

In addition to contending that the settlement agreement did not license future activity, plaintiff seeks to vitiate the settlement agreement on two theories. First, it pleads what amounts to a fraudulent inducement claim. Secondly, plaintiff pleads a breach of contract claim.

The crux of the claim that the settlement agreement was fraudulently induced involves allegations that the defendants denied the allegations appearing in plaintiff's

demand letter quoted above and continued to deny that any misappropriation had occurred during the settlement discussions. Plaintiff contends that the plaintiff relied upon these denials as representations. Any reliance plaintiff may have placed upon these representations, however, would not have been reasonable. In *Pettinelli v. Danzig*, 722 F.2d 706, 710 (11th Cir. 1984), the court said:

> When negotiating or attempting to compromise an existing controversy over fraud and dishonesty it is unreasonable to rely on representations made by the allegedly dishonest parties.

While plaintiff's original claim did not involve fraud and dishonesty in those terms, it did involve allegations of similar conduct, and any reliance plaintiff may have placed upon the denials of wrongdoing at the time would not have been reasonable under the circumstances.

In a similar case from the California Court of Appeals, plaintiff attempted to rely on the merits of its claim to establish fraud in order to set aside a previously entered settlement agreement. The court held

> A party to a settlement agreement may not seek to rescind it by proving the merits of his original claim and then establishing that an erroneous assessment by him of that claim led to the settlement.

A.J. Industries, Inc. v. Ver Halen, 75 Cal. App. 3d 751, 142 Cal. Rptr. 383, 388 (1977).

Plaintiff further pleads that there has been a breach of the settlement agreement by the defendants; that is to say, the defendants have failed to return proprietary, confidential and copyrighted information and materials to SDP. In this regard, plaintiff attempts to characterize

the settlement agreement as an executory accord rather than a substituted contract. An executory accord provides for the acceptance in the future of a stated performance in satisfaction of the antecedent claim. Because the defendants have not fully complied with the terms of the executory accord, plaintiff reasons, plaintiff's remedy is an action on the original dispute, and not an action for damages for breach of the settlement agreement.

In *W. T. Ferguson Lumber Co. vs. Elliott*, 171 S.C. 455 172 S.E. 616, 618 (1934) the court said:

> On the breach of a contract for compromise which has been partly performed the remedy is an action on the contract for damages for the portion remaining unperformed, and the party cannot repudiate the contract and rely on the original cause of action.

After carefully studying the settlement agreement and the various affidavits and depositions which have been furnished to the court in connection with the proper interpretation of the agreement, the court concludes that the agreement did, in fact, constitute a substituted contract as to all claims which existed as of May 31, 1983. The provisions for the return of certain materials subsequent to the execution of the agreement, while valid and enforceable, are not provisions that would make the agreement under consideration an executory accord. Consequently, although the failure to return these materials may well give rise to a cause of action for a breach of the settlement agreement, they do not serve as a basis for abrogating the settlement and allowing plaintiff to renew its original contentions of misappropriation which occurred prior to the date of the agreement.

In light of the foregoing, it is apparent that certain counts of the complaint must be dismissed in their entirety; certain counts remain viable in their entirety; and certain counts must be limited to acts of infringement occurring after May 31, 1983.

Based upon the foregoing, it is hereby ORDERED that the following counts are dismissed in light of the court's ruling pursuant to Rule 56(d): Count IV, Count V, Count IX, Count X.

It is further ORDERED that the following counts remain viable in their entirety: Count III, Count VI, Count VII, Count VIII.

If is further ORDERED that, by reason of the settlement agreement entered by and between the parties, the following counts shall be limited to any acts of infringement occurring after May 31, 1983: Count I, Count II, Count XI, Count XII, Count XIII, and Count XIV.

It is further ORDERED that all motions for summary judgment are denied, that the material facts set forth in paragraphs 1-5 at pages 7 and 8 of this order shall be deemed established, and that the trial of this case shall be conducted accordingly.

IT IS SO ORDERED.

/s/ Joe F. Anderson, Jr.
Joe F. Anderson, Jr.
United State District Judge

Greenville, South Carolina

August 7, 1987

A TRUE COPY
ATTEST: ANN A. BIRCH, CLERK

BY: /s/ M. Campbell
DEPUTY CLERK

APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA

SPARTANBURG DIVISION

J M SMITH CORPORAION, d/b/a SMITH DATA PROCESSING, Plaintiff, -versus- 1. pc I CORP., 2. HILL PHARMACY GROUP, INC., 3. KENNETH A. HILL, 4. W. K. ENTERPRISES, INC., 5. WES KING, 6. RICHIE S. LYNN, d/b/a RICH-2 PHARMACY CONSULTING SERVICES 7. PROFESSIONAL SYSTEMS S.E., INC., 8. A. RODNEY ASHBAUGH, 9. DR. T. C. SMITH COMPANY, Defendants.	Civil Action No. 85-1926-17 Greenville, South Carolina February 18, 1988

TRANSCRIPT OF MOTIONS

BEFORE: HON. JOE F. ANDERSON, JR., U. S. District Judge, presiding.

TRANSCRIPT ORDERED BY: RALPH BAILEY, Esq.

APPEARANCES:

FOR THE PLAINTIFF:	BAILEY & HARDAWAY By: RALPH BAILEY, Esq. JOHN HARDAWAY, Esq. 125 Broadus Ave. Greenville, S. C. 29601
FOR THE DEFENDANTS:	HAYNSWORTH PERRY BRYANT MARION & JOHNSTONE By: JESSE BELCHER, Esq. P.O. Box 2048 Greenville, S. C. 29602
FOR THE DEFENDANTS:	GANDY MICHENER SWINDLE WHITAKER & PRATT By: MACK ED SWINDLE, Esq. 2501 Parkview Dr., Suite 600 Fort Worth, Texas 76102
(Dr. T.C. Smith only)	DAVID D. ARMSTRONG, Esq. P. O. Box 10388 Greenville, S. C. 29603 WILLIAM C. FRUE, JR., Esq. Suite 1102, Northwestern Plaza Asheville, N. C. 28801
COURT REPORTER:	E. Jackie Cole, RPR P.O. Box 10732 Greenville, S. C. 29603

Proceedings recorded by mechanical stenography; transcript prepared by computer-aided transcription.

(p. 3) THE COURT: Morning, gentlemen, this is the case of *J M Smith Corporation versus pc I Corporation* and others, before me upon motion of the defendant for partial summary judgment on certain issues that we'll explore in just a moment. Of course back in July of last year we heard about four hours of oral arguments and I certainly don't plan to repeat that today. I think I understand the issues and have reviewed your memorandum and looked at some of the authorities you've cited. The basic question, as I understand it presented by this motion, is really a subsidiary question I guess really wasn't addressed in my summary judgment order. I think the parties had really explored this derivative work issue at the hearing and I just kind of glossed over it in my order, but I agree with you it does need to be resolved, and as I understand it, my order simply indicated that as of March 31, 1983 –

MR. SWINDLE: May 31.

THE COURT: May 31, 1983 there could be no claim by the plaintiff for any infringement that occurred prior to that date, but that any copying which occurred subsequent to May 31 would be actionable. That leaves open the question of derivative works. Apparently it is the contention of the plaintiff that derivative works were not permitted either under the settlement agreement. Let me hear from the defendants at this time.

(p. 4) MR. SWINDLE: Thank you, Your Honor. Mack Ed Swindle on behalf of the defendant, Your honor.

THE COURT: Good to have you in South Carolina.

MR. SWINDLE: Thank you, Your Honor, good to be here. Your Honor, this theory which plaintiff is asserting we believe is frankly new theory, and I think that is one reason the Court has not a addressed it in earlier order in any detail.

THE COURT: Didn't we discuss it at the last hearing though?

MR. SWINDLE: Not appreciably. Frankly, as I look at it, it is something they brought up kind of on the rebound, and I'll explain why in just a moment. What they seem to be saying is that in the settlement agreement the defendants obtained only an implied license to use the pc I product as it existed on May 31, and the defendants did not have the right to change the product, could not update it, couldn't maintain it, couldn't support it, couldn't change it in any way, or it became an infringing derivative product. I think that is clearly in contravention of established law and that is what I want to argue in just a few minutes. I don't think it will take long to do that. The foundation of their argument is that the settlement agreement gave an implied license. That is the foundation, and if that foundation does not exist, the argument has no (p. 5) foundations. So without the Court finding that the defendants are simply implied licensees, the only conclusion can be reached is that the pc I product can be updated, modified, changed, added to, so long as it is not done with infringing work. In other words, we can add to it from something we write. But we're not suggesting to the Court that we have the right to go copy it in order to update our product. So what is not addressed in this motion is whether or not we infringed them after May 31,

1983. We had denied that we did, but that is something clearly for a factual determination.

THE COURT: I think that is purely factual issue, I noticed in the footnote allegations that what, nursing home codes and other –

MR. SWINDLE: I don't know what all they claim, Your Honor.

THE COURT: Then got patient counseling codes, I indicated before I have some real problem with.

MR. SWINDLE: On patient counseling codes, which is another work, Your Honor, on drug file, separate work from the system; that is another issue, fact issue at the trial, not addressed in this motion. What the plaintiff's argument is that the product, pc I product, became infringing as a derivative work and it is based on a faulty assumption. The assumption is that the complaint the (p. 6) plaintiff made back in May of 1983 was legitimate.

THE COURT: What was the complaint they made?

MR. SWINDLE: They said: "pc I, your product", in the words of Mr. Manning's demand letter, "incorporates significant portions of QS/1's system." That was what was denied. Reason it was denied is for the history of the development, which the Court already noted. I won't do but maybe 20 seconds of the history, but again just to say it, the pc I product came from G/H Plus product, which was written by Gilstrap and Hegeman at the time they owned QS/1 and the time they owned Gilstrap 32, the first product Gilstrap 32 QS/1 came from that derivative product. At the time they owned QS/1, they wrote G/H Plus. They then sold QS/1 to SDP and retained G/H Plus

and Gilstrap 32. Then they let Zadall, in Canada, write a new product off the G/H Plus product, which became pc I. All of that history was the basis upon which pc I in 1983, said, "No, we're not infringing on you, SDP; here is where our product came from, you're welcome to look at it in detail." Those were the issues in '83. That is what led up to the settlement agreement dated May 31.

THE COURT: I want to stop you there. Exactly what consideration changed hands in the settlement agreement? I should know from the last hearing, but it didn't seem like to me either side gave up much, almost a (p. 7) call it quits go home type thing?

MR. SWINDLE: Your Honor, I think your order expressed it best on page 10 – 9 of your order, when you pointed out the consideration. One is in exchange for the release, pc I changed its trademark. That was a substantial piece of consideration because we had already started using that trademark in the publications; we had all of our advertising data. It was a substantial change. Any time a company obviously changes trademark we pay for it. We had to do all kinds of republications, reprinting. Number two, we gave back to SDP, the defendants, the rights to distributorship contracts, which we had with users of QS/1 under which we had the right to obtain a lot of money, maintenance agreements, and we got monthly maintenance. A lot of money we were giving up, but we did that in exchange for basically severing our relationship. There were one or two additional ones, but I think those are the most prominent.

THE COURT: No actual money changed hands.

MR. SWINDLE: No actual money either way, that's correct, except –

THE COURT: Well I was, of course, a little bit rusty on facts of the settlement agreement obviously, but I was mentioning to my law clerk before we came out, I was wondering what the plaintiffs got in 1983 to cause them to (p. 8) settle. What you're saying is they got something of substantial value.

MR. SWINDLE: They certainly did, and we gave up something of substantial value as well, hurt our pocketbook and helped theirs, because they got those maintenance contracts.

Now after the settlement agreement then, where do we stand? Well for two years, we are out in the marketplace, updating our product in what we believe to be a non-infringing way, rewriting, we've got our on own programs. Then two years later, after not having heard a word from them, get sued. Basically they sue us saying the same thing they said back in 1983. You guys have included significant portions of the QS/1 product in pc I and we said we settled that. They said, "no, the settlement agreement came about by fraud" and they asserted that for two years of litigation until finally this Court found that the settlement agreement could not be set aside because of fraud for obvious reasons no reliance, and other reasons set out in the Court's order. So now what they have done is they've taken it to a new theory, where they say, "okay you may have had the right to use it" – previously they maintained we didn't have the right to use, somehow we were settling, but we couldn't use it

anymore. Now they said, "okay you have a right to use it, but you don't have the right to change it". (p. 9) Okay.

Well where do we stand with that? There is some admissions the plaintiff have made which I think are real important in their brief. They have said the use by G & H of G/H Plus does not infringe QS/1. G & H could permit derivative works of G/H Plus if they want to, and that would not infringe QS/1. And that is what has happened. G/H Plus has a derivative work, pc I. That has been our position from the time they made the first demand upon us. Now what the plaintiff argues is: "We don't think that happened. We think you copied our system. And so we base our claim of infringement, our claim that you cannot change your product or it becomes an infringing derivative, work upon our claim that you have copied our system." That is the basis on which they claim that we don't have the right to change it. Only one response to have to that. That is what was settled. We would have defended this case in 1983 on the grounds that we had a derivative product of G/H Plus, and we've gone back through the history of that previously, but the biggest obstacle that the plaintiffs have to overcome and the one they cannot overcome as already evidenced by the Court's ruling, is the settlement agreement. That then becomes a wall beyond which they can not go. And there is no reason then for us to get into the issue of whether or not our product is a derivative of G/H Plus, or a derivative (p. 10) of QS/1. Obviously we've gone into it in discovery, we've briefed it for the Court, presented it in the summary judgment, and I think pretty well established we are a derivative of G/H Plus, not QS/1. But that is the problem with their argument.

THE COURT: Can you tell me, Mr. Swindle, in laymen's terms what some of the changes are, give me an example?

MR. SWINDLE: Yes, Your Honor. As this product is sold to a user, a pharmacist, he will come up with an idea, as a user, and say for example, "okay I'm in the pharmacy filling portion of the system and I want to fill a prescription and so I have got the name of my customer and I got the drug and typing in the drug, and as I do that, I wish there were some way, pc I, you could make it so that at the end of the day, I can have a listing of all the customers I filled on that given day. Would you write a subpart of your system that just takes that data and stores it in say we call X file? Would you do that so at the end of the day I can go back and say I filled prescriptions for John Doe, Richard Row, Jim Smith, whomever." pc I will take this information from the field and say "that looks like a good idea." Give it to the programming staff and say how hard is it to do that? Programming staff will see and then come out with updated release of the product. We ship (p. 11) these diskettes out to the user, he'll just plug that into the system and will print, not print but take from diskettes on to his hard disk this data, hook it into the system so it becomes an updated product. That is the way it works from a practical standpoint.

Now let me get back, this is really, Your Honor, not a copyright question, as the Court has before it. This is a contract question, simply a contract question, because what we're talking about is what does to release mean? The release gives something. The question is does it reserve something. The plaintiff seems to be saying that the settlement agreement reserves some kind of right, doesn't

say anything admittedly, but they say the contract only gives pc I implied license. The settlement agreement is before the Court and attached to our answer. It is also obviously attached to the summary judgment. But what does the settlement agreement say? It says SDP releases all past and present claims it has against pc I and defendants, basically, relating to pc I Pharmacy System. That is the language. What does that language then say about implied license? Doesn't say anything. What does it say relative to what rights have been granted to pc I? Doesn't say anything. What does it say about rights reserved? Says nothing. What we have then is the plaintiff saying, "we were giving an implied license." And we're saying, "No, (p. 12) what we had was a copyright in our system, we own it, it came from G/H Plus and we own it; when you wrote a demand letter, you put a cloud on it. But when you settled it, you removed the cloud, you didn't give us anything. Our rights don't come from the settlement agreement, our rights come from our own copyright, our own right, all you did was remove that cloud when you released it.

Now, the Court will recall if you go back to the brief the plaintiff originally filed, plaintiff said there was no license granted. Their earlier lawyer says there was no license granted, said three time as I recall in their brief, and properly so. We believe that was a proper statement, they properly briefed that question. There was no license granted by the settlement agreement.

Now, the plaintiff is relying upon the case of *Oddo versus Ries* and in this case, *Oddo and Ries* formed a

partnership, and Oddo had written some magazine articles and had written some manuscripts from those magazine articles, contributed the manuscript to the partnership, then the partnership split. When the partnership split, Ries then took the manuscript, used it the with another author and wrote a book from it. Oddo sued, saying the manuscript belongs to me. The Court pointed out that this was an accounting case from the dissolution of the partnership and the Court found that when Oddo gave the partnership the (p. 13) manuscript, the partnership had the right to use this manuscript. There had to be some kind of implied license granted when he gave the partnership the manuscript. So the Court said we find there is implied license, but we don't find that that license is broad enough to give Ries the right to take that manuscript and write a book from it to become a derivative work after dissolution of the partnership. That's what *Oddo/Ries* stands for. The reason the Oddo versus Ries case is distinguished from our case is number one, Oddo gave something to the partnership and the implied license arose. In this case SDP has given pc I nothing. All they did in 1983 was say "you're infringing" and we settled. That was simply a release. The *Oddo/Ries* case does not involve a license or release. For them to try to apply the *Oddo/Ries* case to this case, would call for an absurd result. Let me show how absurd it would be. Let's say I own a horse, for example, and Mr. Bailey says, "Mr. Swindle, that's my horse." And I say, "No, it is my horse" and we got a dispute and I say, "but tell you what, Mr. Bailey, I'm going to give you hundred dollars if you'll go away and drop your claim." He says, "okay", and he

leaves and he signs a release releasing me from claim he's made.

THE COURT: I had a case very similar to that one time if you can believe, I actually represented a horse thief.

(p. 14) MR. SWINDLE: Maybe I'm using the wrong case.

THE COURT: A little more complicated than that, but go ahead.

MR. SWINDLE: But assuming each of us thinks its our own horse; he pays his hundred dollars and releases me. Then I take the horse and I use the horse to plow or I use the horse to race, and he comes back and says, "Mack Ed, that horse you using to race, I thought you were going to use to plow." I say, "no, we didn't say anything of that sort in our agreement you just released." He says, "well I didn't give you the right to race her"; or he may say, "you got a foal from that mare, I didn't give you the right to that, I want to keep it"; and I would have to say, "Mr. Bailey, the release is simply a release; you said you owned the horse, and you released that claim, we can't go behind that because you got the consideration and the release." That is the kind of result that would occur if the plaintiff were allowed at this point to try to go behind the settlement agreement. It would undo the settlement agreement. We would have to try the trademark issue here; we would have to try the issue of what kind of damages we suffered by way of having to give up our rights to maintenance contracts. We would have to go way behind the settlement agreement. Critical thing is,

had that been the intention of SDP, they were well represented by counsel, (p. 15) previous counsel in this case, and would have reserved those rights. They would have said and Mr. Manning is a copyright lawyer and he would have said, "If we release you from all claims, pc I, but you have no right to modify the program." Or he would have said you have no right to sell your program, if his earlier contention had been correct. But none of those were stated. So all this really boils down to is we have a settlement agreement, plaintiff tried to go behind initially by saying it came about through fraud. The Court addressed that and now they're saying "you can use the product, but you can't change the product." They knew we were going to change the product. That is common knowledge in the industry. Even the settlement agreement, page one, says: "Whereas SDP is the owner of QS/1, which SDP continues supports and update." It's common knowledge in this industry you update these products. So that was well within the intention of the parties, witnessed in the recital of the paragraph in the first page. So what we've got then really –

THE COURT: That is problem with this case. I mean that is the reason this issue is so difficult to get a handle on, computer programs change so much, not like a book and question whether you use as book or comic book or something always had a potential. Just like trying to hold on to mercury or water, something, just never the same.

(p. 16) MR. SWINDLE: That's correct, these are continually changing. Now Your Honor, we have no reason to claim today that you have to say we have the right to change it to include infringing matter. We're prepared to defend that at trial. But the only issue is do we have

the right to change it with non-infringing matter. We believe we do, not because of a bunch of copyright issues, simply contract law. So what claim did the plaintiffs have, if any? What claim did they release in 1983? What claim did they reserve? Those are the issues, and those are addressed by the contract. That determination can be made from the release, and that is all we asking at this point.

THE COURT: The language of the release said all past and present claims of infringement, words to that effect.

MR. SWINDLE: That's correct.

THE COURT: Really didn't address derivative works one way or the other.

MR. SWINDLE: Your Honor, the question is what impact does derivative works have on this. The plaintiff, I think is saying, "you have a derivative work but derivative work of our product." And we say, "No, that is what we settled. Ours is a derivative work of G/H Plus product and we have a right to our own copyright. I think they are trying to, frankly, I think they are trying to muddy the (p. 17) water by bringing in a derivative work question and it's nothing more than a contract question. The derivative work question is at best their best authority the *Oddo vs. Ries* case, one they cite, and that doesn't have any application in this case. So it is not a question of do we become an infringing derivative work. Certainly we're derivative work, but of G/H Plus and Gilstrap 32. They are as much a derivative work as we are of Gilstrap 32. So that's the situation. Contract question, what was

released and what was reserved? The contract tells us. Thank you.

THE COURT: Thank you, Mr. Swindle. Mr. Bailey.

MR. BAILEY: May it please the Court, I'll try and get directly to the point, be brief, because we respectfully submit that contrary to the defendants' position there is nothing new or esoteric about the point being made in this case. In 1982, when Smith Data Processing obtained a license from G & H for the then existing drug file, it was specifically provided in it that SDP may modify the said code at its discretion. Everybody knows that the rights in a copyright are considerably different from the bundle of rights that the owner of a horse possesses. Section 106 lists a number of rights in the bundle of rights owned by the copyright proprietor. Among them is the right to reproduce, but there is also the further right to make a derivative work. And the cases are (p. 18) clear that unless that right to make a derivative work is licensed by express agreement, then there is no right to make a derivative work. And I would ask Your Honor to consider what the posture of the parties was at the time of the settlement in this case. Very little consideration flowed to the plaintiff. The plaintiff wanted to get away from the trademark; the plaintiff didn't think that with the pc I program in its incomplete state at the time of the settlement they could be a real factor in market. But suppose the defendants, suppose pc I had said "Now we're going to include in this settlement agreement the right to modify, the right to add whole sections, right to add nursing home, the right to add narcotics and controlled drugs, the right to add sales analysis, not only the right to update, but the right to add, all these sections"? I don't believe

they would have made that settlement, and I don't think it's up to the Court to make that settlement for the parties at this late date.

Now, counsel says that pc I is a derivative work of G/H Plus and well it may be, but it may be a derivative work of more than one pre-existing work, and the definition of derivative work in the code in section 106, I beg your pardon, section 101 is quite clear that a derivative work is a work based upon one or more pre-existing works. And we have no quarrel with their making a derivative work of G/H (p. 19) Plus, but where QS/1 is part of the derivative work, then we do.

THE COURT: So it is your position they do have the right to produce derivative work of G/H Plus, but not QS/1?

MR. BAILEY: Exactly, Your Honor. And it is not the work, pre-existing work comes from G/H Plus that we complain about. It is the work that was copied from QS/1 at time of settlement that was in pc I. And then using that as a pre-existing work and adding to it. That is what we complain about. And this is the case of *Oddo versus Ries* is precisely on point. Counsel says this is a contract case. Yet the authorities, *Oddo vs. Ries* and *Gallium*, speak of infringement, they speak of tort. Not a contract case at all, this is a question in tort.

THE COURT: I think his point is the contract settled the tort claim, settled infringement claim. I'm not saying I agree, but I think that was his point.

MR. BAILEY: Our point is the contract never did that. Contract was silent and this Court gave, recognized

a right of some kind in the defendants to future activities as a result of the settlement on the trademark. The defendants agreed to take the slash out of pc I so as presumably not to be confusing with GH slash Plus, in order to get away from the trademark. They, by agreeing to that, this Court held (p. 20) that the defendants had a right, license or a right of some kind to future activities with the G/H Plus program as it existed at the time of the settlement. There was no express agreement one way or the other as to whether or not a derivative work could be made. But the cases say that there must be an express agreement. In the absence of express agreement there is no right to make a derivative work, and in the absence of license or some sort of right in the, this Court found to exist, in the settlement agreement, then the defendants wouldn't have a right to do anything. Presumably the defendants were going to make their own program after this settlement, and they going to be able to use pc I as it existed at that time until they could make their own program.

THE COURT: Let me ask you one point, I hate to interrupt, to be sure I understand where we are. Do both of you agree that this is a legal question at this time or are there?

MR. SWINDLE: Yes, Your Honor.

THE COURT: Is potential for factual disputes that would make summary judgment inappropriate? Obviously you say not, Mr. Bailey, do you think –

MR. BAILEY: Certainly there is a factual dispute, Your Honor. That is whether or not pc I contains QS/1's pre-existing works. Counsel, as I understand, denies that.

(p. 21) If counsel admits that, then it is indeed a question of law and this Court can give judgment for the plaintiff presumably should we follow up with a motion of our own.

THE COURT: So it is your position, in short is, that because the agreement was silent on the question of derivative work, because the substantive law of copyright requires that it expressly be granted, that there is some type of implication here that there was no –

MR. BAILEY: Precisely correct, Your Honor, and our position is further that this is nothing new or esoteric. It is right in this copyright statute. The case of *Oddo versus Ries*, as counsel stated the case, I think the facts are a little bit different. The pre-existing work the *Oddo versus Ries* was magazine articles which Oddo had written. Oddo, pursuant to his agreement with Ries, took these magazine articles, rewrote them, supplemented it, and got a manuscript, which he submitted to Ries for potential publication. Ries wasn't satisfied with the progress he was making on the work, so he in effect fired Oddo and hired a new author to finish the book. Now what the Court held was that as far as publication of the manuscript was concerned that Ries had a right to use the pre-existing magazine articles which Oddo had a copyright on, but that he did not have a the right to use those magazine articles in a book, a derivative work in other words,. The *Oddo/Ries* could not (p. 22) possibly be more in point; it is absolutely on all fours with the facts in this case.

THE COURT: All right.

MR. BAILEY: And *Gillium* case, the monophthong that Professor Nimere spoke of, holds the same thing,

doesn't make any difference whether the license to reproduce is expressed as it was in *Gillium* or implying as it was to Oddo. It's the fact that there is no express right to make a derivative work that is important, and that is what the law requires an express right to make a derivative work.

THE COURT: Let me ask Mr. Swindle. It did seem to be a distinction between the case of derivative work, right to make a derivative work must be expressly granted.

MR. SWINDLE: That's correct, Your Honor, we agree with that. The distinction is and the leap of logic which counsel is overlooking is that in *Gillium* case, monophthong was admittedly the owner of the matter in question. In *Oddo vs. Ries,* Oddo owned the articles; the partnership owned the manuscript, and Ries had taken a derivative work of something he had only a license in. In both of these cases there was license, and that is all there was.

THE COURT: Here there was dispute at the time that never was resolved one way or the other; it was just settled.

MR. SWINDLE: Exactly. And that's why there is (p. 23) not a fact question. There would be a fact question had the settlement agreement not been in place, because we would have a dispute as to whether or not our system came from G/H Plus, as we say, or from QS/1, as they say. But that is the issue that was settled. That is why there is not a fact issue. May I continue briefly on that point? Counsel has said, Your Honor, that unless you have the right to make a derivative work expressly given

in the contract, it does not exist; and that is true, but that is the second step of the argument. We don't get there. The first step is: was there ever a license? Was there ever an implied license? I challenge counsel to show is why there is implied license and only implied license granted by the settlement agreement. We are not relying upon implied license or express license. In order for that settlement agreement to provide for an implied license, it would have to be an acknowledgement, have to say "pc I acknowledges that QS/1 is the product from which it came." And yet because of the release now pc I has the right to go out and market its product. That would be a license. That would give an implied license. But that is not what it says. It simply says SDP made a demand; you stole our product. We say we did not; and they said "we release all claims." Which claims did they release? They released that claim. That is the one that was released. Simply a contract question.

(p. 24) THE COURT: All right.

MR. BAILEY: May it please the Court, we respectfully submit a settlement agreement is no different from any other kind of agreement, and that whether the license to reproduce is expressed or implied, makes no difference. The point is that the right to make a derivative work, right to make modification, right to make appreciable departure from the work as it is licensed, must be something that is expressed. In the settlement, in the agreement, whatever it is, settlement agreement, an implied agreement or some other kind of license or right, that right must be spelled out. And the parties, it is a very important part of this settlement, I respectfully submit, that the plaintiff never thought that defendant with the

program that they had as incomplete as it was could have made it in the marketplace, particularly if they were distinguished from their trademark, and I don't believe they ever would have settled it, if the right to make modification and additions to that program had been included in that settlement agreement. I don't believe they would have settled.

Now, as far as whether or not G/H Plus or QS/1 was the pre-existing work for pc I, as counsel seems to indicate, that wasn't the issue at all. The issue was whether or not QS/1 was the pre-existing work, whether or (p. 25) not that work was copied, and that was never decided. It was simply, was simply a settlement that the program as it existed, pc I as it existed, at the time of settlement, could be reproduced. Surely the settlement agreement goes no further than that. Even that right had to be found, because of something involving the trademark issue, which was settled by that settlement agreement. The agreement is totally silent, settlement agreement is totally silent as to any right to make a derivative work, as to any right to make modification or appreciable or substantial departure from pc I as it existed at that time. And I think as the parties, if the plaintiff had envisioned that the defendant would do that, if he had been asked, if the plaintiff had been asked to include that in the agreement, I don't think they would have done it.

THE COURT: Mr. Bailey, so it is your position as of the day the settlement agreement was entered, the parties agreed that the defendant could use their system, their pc I system or pc I, whatever I can't keep these names straight, they could use it as it existed that day, with no changes whatsoever.

MR. BAILEY: Your Honor, and I think this is a fact question whether or not changes make pc I a derivative work, whether or not the changes are that extensive. Now that is issue for the trial of this case, regardless of who (p. 26) made the changes, whether or not they are sufficiently extensive.

THE COURT: That is my point.

MR. BAILEY: To bring into being a derivative work.

THE COURT: That's the point I was trying to get to.

MR. BAILEY: The *Gillium* case speaks to that point, and says here, Your Honor, this is on page 23 of 538 F.2d:

> "Courts have recognized that licensees are entitled to some small degree of latitude in arranging the license work for presentation to the public in a manner consistent with the licensee's style or standards."

That privilege however does not extend to the degree of editing occurred here, especially in light of contractual provision that undertook the right to edit monophthong material. Now Your Honor, far more has occurred here than merely editing, than merely keeping this program up-to-date. The program was incomplete at the time of the settlement agreement. Now on page 6 of the defendants reply brief, it is stated this was over four years after the settlement and followed tremendous further development of pc I, which obviously significantly increased its salability, resulting (p. 27) in the sale of literally hundreds of systems. Now, this is the question. Hadn't been many sales at the time of settlement and plaintiff was willing to continue, provided they continued under another trademark or using their own program.

THE COURT: This was about the time many micro computers was beginning to takeoff, about the time settlement agreement was entered.

MR. BAILEY: That's right.

THE COURT: And assume the defendant experienced a big boom in sales after settlement agreement.

MR. BAILEY: The question, fact question for the Court at the time trial is whether or not there has been sufficient modifications of the pc I work as it existed at the time of trial to constitute a derivative work. Now while some small amount of modification may be contemplated, it was not contemplated the whole sections were going to be added.

THE COURT: I agree that might well be a factual question – wait a minute – whether this was small degree of latitude that you quoted from the case, or broad enough to be a derivative work. Mr. Swindle says, even if it was broad changes constitute derivative work, under the law they have a right to do that. Still kind of back to a legal question before me, it seems.

(p. 28) MR. BAILEY: I think that's right, Your Honor. The question is really what law applies more than a question of whether or not some sort of judgment is going to be granted by the Court.

THE COURT: All right. You have anything to add?

MR. SWINDLE: Just a couple things, Your Honor.

MR. BAILEY: I'm sorry, Your Honor, I wanted to add that the question is whether or not we have to show that the additions were copied or whether they were

merely sufficient additions, regardless of who made them, to constitute pc I a derivative work.

THE COURT: All right. Mr. Swindle, anything very briefly.

MR. BELCHER: Could we have just a moment.

MR. SWINDLE: Two or three things very briefly, Your Honor. Mr. Bailey argued outside the record a little bit, frankly incorrectly – not critical of that because a big record, but he was speculating a moment ago what might have happened if the parties had said what we want from SDP is right to change our product. Well, there is testimony and it is in the summary judgment briefing that has been done. Mr. Hammond, president of SDP, said "I knew they were going to sell, I knew it was incomplete", clearly it was within the contemplation of the parties it was going to be changed, going to be updated.

(p. 29) THE COURT: If it was incomplete at that stage, they gave license – not a license, gave permission to continue using it, with a new trademark, you could argue there was a contemplation would be modified.

MR. SWINDLE: Certainly. Even assuming his theory, even assuming his theory that we were derivative of of QS/1, but, you see we don't get to that point even and that is why there is not a fact issue, because they were saying "You are a derivative of" – at that point they were saying, "You're infringing derivative of QS/1, we don't care where you came from, you have our product, you have included significant portions." They were saying you're infringing derivative. And we said, "no, we're not." And they said, "We release it for the consideration

given." That is why it's not a fact issue. He has also ignored the plain language of the agreement, Your Honor. This statement that, this argument that there is a fact question as to whether or not there was sufficient modification in pc I to become a derivative work is not a fact question either, not a fact question that will cause us to get around this hearing. Because to get to that fact question you have to again assume that we were a derivative of QS/1; that is what was released. So we don't even get to the question of whether a derivative work is authorized, how much is authorized, how much modification we have to do to be a derivative work. (p. 30) Only question is what was released. They were saying you infringing. Could have said you infringing derivative work as easily. We said, no we're not, that is what was released. Trying to go behind the settlement agreement again, whether for limited purpose or otherwise, and they are not permitted to do that. That is why it's simply a contract question.

THE COURT: Thank you.

MR. BAILEY: May I respond just briefly to that, Your Honor. The complete answer to counsel's argument is found in the fact the cause of action, the thing we are – position that we're taking now, the infringement that we are complaining of didn't take place until after the settlement agreement. These, the derivative work did not come into being until after the settlement agreement. That is what we're complaining about. That is what was not covered in the settlement agreement; that is the thing has to be expressed. And all the cases hold that. And it is the thing that I respectfully submit the parties, the plaintiff

would never have countenanced in the settlement agreement. Now, it's true that I may go beyond the record on that point, but consider it hypothetically. And the reason I go beyond the record is because I think counsel did that in his argument. But considering that hypothetically, that is an important consideration that a plaintiff would have in (p. 31) entering into a settlement agreement of the type involved in this case.

MR. BELCHER: Could I make one, promise you I will be brief. The Court had earlier in its comments indicated that what was released was past and present claims of infringement, and the operative language of the release is not precisely that.

THE COURT: Maybe I misspoke.

MR. BELCHER: It says, "all the past and present claims that the plaintiff may have relating against the defendants, relating from their individual and collective activities relative to the pc I pharmacy system." Obviously, just as they are asserting here today, that you got no right to make a derivative work of it. That was a claim that they may have had, and in fact did have at the very time this settlement agreement was entered into. Now, it is that claim in the generic sense that has been waived forevermore. It has been waived. They had the right to make the claim, and in effect did make the claim about derivative works. And that is one they could have made and in the context of the claim they may have, and it has been settled.

THE COURT: All right. I think I heard enough, gentlemen, Mr. Bailey.

MR. BAILEY: I would just like to respond to that, (p. 32) one moment. The derivative work we're claiming didn't even come into being until after the settlement agreement; couldn't possibly have been covered by it. If there is to be any derivative work, the cases and statute are clear there has to be expressed agreement.

THE COURT: All right. Gentlemen, I tried to listen to you extensively this morning, read your memoranda you submitted. I think both sides did a very good job in the limited amount of time I gave you.

I'm going to grant the defendants' motion. I may be wrong, but I have great faith in the settlement that entered back in 1983. I do think that since it probably will be appealed, potentially could be appealed, I should expound on my decision in a written order which I will do so. I have got to leave in about hour to go to Columbia for the rest of the day, so it may be first of next week or midweek before we get something out. But my review, and I did make a sincere effort to review the file, has been several months since I looked at it, but I did look at the record, my earlier order, and I reviewed your memoranda. I don't think there is a factual issue involved on this particular point, and I do feel as a matter of law the settlement agreement did not prohibit the right to make additional derivative works and I will expound on it in written order next week.

(p. 33) MR. BAILEY: May I ask a question. One issue I think should be resolved, as far as trial is concerned, may we offer evidence concerning the extent to which QH, QS/1 was copied into pc I at the time of the

trial for the purpose of laying the groundwork and to show a pattern of copying.

THE COURT: Certainly I will permit you to make an offer of proof, Mr. Bailey. I don't guess that is something you could stipulate.

MR. BELCHER: Your Honor, I don't think we can. And I would like to alert counsel to the fact we are seeking attorneys fees for the breach of settlement agreement. So efforts, you know, are persisting to go behind the settlement agreement, you know.

THE COURT: I understand that, but I certainly have to permit plaintiff to make a record of what the evidence will be. It may be that rather than putting up days and days of testimony, if you could summarize it, make an offer just an offer of proof or statement into the record of what you would be prepared to prove.

MR. BAILEY: Your Honor, our purpose is showing a continuing pattern of copying. They copy up until the settlement agreement and they copied after the settlement agreement, and that is the purpose of the testimony.

THE COURT: We'll permit you to do that certainly, (p. 34) all right, thank you.

I certify that the foregoing thirty-four (34) pages is a true and correct transcript of the proceedings as recorded by me stenographically and transcribed to the best of my ability.

/s/ E. Jackie Cole — Official Court Reporter

Jan 5, 1989 — Date

APPENDIX E

UNITED STATES COURT OF APPEALS

FOR THE FOURTH CIRCUIT

No. 88-3181
(FILED JAN 22 1990)

J M SMITH CORPORATION, d/b/a Smith Data Etc. Processing

Plaintiff – Appellant

v.

PC I CORP; HILL PHARMACY GROUP, INC; KENNETH A. HILL; W. K. ENTERPRISES, INC; WES KING; RICHIE S. LYNN, d/b/a Rich-2 Pharmacy Consulting Services; PROFESSIONAL SYSTEMS S.E., INC; A. RODNEY ASHBAUGH; DR. T. C. SMITH COMPANY

Defendants – Appellees

No. 88-3186

J M SMITH CORPORATION, d/b/a Smith Data etc. Processing

Plaintiff – Appellee

v.

PC I CORP; HILL PHARMACY GROUP, INC; KENNETH A. HILL; W. K. ENTERPRISES, INC; WES KING; RICHIE S. LYNN, d/b/a Rich-2 Pharmacy Consulting Services; PROFESSIONAL SYSTEMS S.E., INC; A. RODNEY ASHBAUGH; DR. T.C. SMITH COMPANY

Defendants – Appellants

On Petition for Rehearing with Suggestion for Rehearing In Banc

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The appellants' petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no

member of this Court or the panel requested a poll on the suggestion for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

Entered at the direction of Judge Phillips with the concurrence of Justice Powell and Judge Hilton.

For the Court,

JOHN M. GREACEN
CLERK

APPENDIX F

SETTLEMENT AGREEMENT

AGREEMENT entered into as of the 31st day of May, 1983, by and between J M Smith Corporation, d/b/a Smith Data Processing, a corporation organized under the laws of the state of South Carolina, and having a place of business at Spartanburg, South Carolina (hereinafter referred to as "SDP"); Hill Pharmacy Group, Inc., a corporation organized under the laws of Texas, and having a place of business at Granbury, Texas (hereinafter referred to as "HILL PHARMACY"); and pc/1 Professional Systems, Inc., a corporation organized under the laws of Texas and having a place of business at Granbury, Texas (hereinafter referred to as "pc/1 Professional").

WITNESSETH:

WHEREAS, SDP is the owner and sole licensor of computer systems for use in pharmacies, which systems include application programs and operating systems for use in conjunction with IBM Series/1 computer hardware, which SDP continually supports and updates, all of which is individually and collectively referred to hereinafter as the "QS/1 Pharmacy System", and with versions of same sometimes referred to as "PDQ" and "P-1" System", and

WHEREAS, SDP considers all of its information related to the QS/1 Pharmacy System that is not disseminated to the general public to be confidential and proprietary information of SDP, and claims copyright in

and to certain of said confidential and proprietary information, including, without limitation, all computer software, operating manuals, maintenance manuals, and the like, and

WHEREAS, SDP long ago adopted and used QS/1 as a trademark for pharmacy systems, which trademark represents valuable good will of SDP, and

WHEREAS, all of SDP's licensees and end users for the QS/1 Pharmacy System have entered into agreements with SDP in which said licensees and end-users have acknowledged the existence of confidential and proprietary information of SDP, have agreed not to disclose same to anyone without the prior written consent of SDP, except to end users who properly execute an appropriate sub-license agreement, and have agreed to take all steps reasonably necessary or advisable to protect SDP's confidential and proprietary information from being made available to any person and to protect SDP's rights therein, said agreements being respectively hereinafter referred to as "License Agreement" and "Sublicense Agreement", and

WHEREAS, Hill Pharmacy, on July 23, 1981, entered into a License Agreement with SDP, and since that time, has continued to operate as a licensee/sublicensor for the QS/1 Pharmacy System, and

WHEREAS, Ken Hill, president of Hill Pharmacy, and others are shareholders of pc/1 Professional, which corporation was originally known as Preferred Professional Software Corporation, and which corporation markets a computer system for pharmacies referred to as pc/1 pharmacy system (hereinafter referred to as "pc/1"), and

WHEREAS, certain of said shareholders are presently licensees of QS/1 Pharmacy Systems under License Agreements with SDP, and

WHEREAS, SDP has alleged that the use of pc/1 as a tradename and as a trademark for pharmacy systems is an infringement of its trademark QS/1 for pharmacy systems; that pc/1 Professional and Hill Pharmacy have misappropriated confidential and proprietary information of SDP and have utilized such confidential and proprietary information in the pc/1 pharmacy system, and

WHEREAS, SDP has made written demands through one of its attorneys, Wellington M. Manning, Jr., by letter dated May 5, 1983 to Ken Hill, president of Preferred Professional Software Corporation to immediately recall all of the pc/1 pharmacy systems and to remove all of SDP's confidential, proprietary, and/or copyrighted information therefrom, and to immediately cease all future use of the tradename and/or trademark pc/1 in conjunction with a pharmacy system, and

WHEREAS, SDP has alleged that Hill Pharmacy is in violation of the License Agreement dated July 23, 1981, and

WHEREAS, by letter dated May 17, 1983 from Glenn Hammett, president of SDP, Hill Pharmacy was notified of the termination of its aforesaid license agreement, and

WHEREAS, pc/1 Professional by letter dated May 12, 1983 from its attorney, Mack Ed Swindle, denied that pc/1 constitutes an infringement of QS/1 for pharmacy systems, denied that Hill Pharmacy was in violation of the aforesaid License Agreement, denied access to any

confidential or proprietary information of SDP, requested specifics as to SDP information that is copyrighted and is considered by SDP to be an infringement, and accused SDP of attempting to subvert in an anti-competitive way a new company which has developed its own product which is not relying in any way upon SDP's confidential or copyrighted material, and

WHEREAS, by letter from Mack Ed Swindle dated May 23, 1983, Hill Pharmacy denied it had breached the License Agreement with SDP dated July 23, 1981, informed SDP that SDP would be in breach of the aforesaid License Agreement if SDP attempts to terminate Hill Pharmacy's license, and alleged possible tortuous interference by SDP with business relationships of Hill Pharmacy, and

WHEREAS, the parties wish to settle their differences without resort to litigation;

NOW, THEREFORE, in consideration of the aforesaid premises and the mutual covenants set forth hereinafter, the parties do hereby agree as follows:

1. pc/1 Professional agrees to immediately cease all use of the designation pc/1 in its tradename and as a trademark or a portion of a trademark for pharmacy or related systems, and further agrees to refrain from any use in the future of the designations /1 or a / followed by a one digit numeral, in combination with a group of letters, or from any use of any other designation, all in conjunction with computer systems for use in pharmacies which would be confusingly similar to SDP's mark QS/1 for pharmacy systems. pc/1 Professional further agrees to immediately change its tradename and trademark(s) to

delete pc/1 therefrom and to use pc I in lieu thereof; to designate its computer system as a "pc I Professional System", and not a "pc I Pharmacy System"; and to use as its logo, pc I with a rose in a horizontal disposition beneath same, all within an encircling, colored border; it being understood, not withstanding anything to the contrary herein, that pc/1 Professional shall have the right to use the trademark pc I. It is further agreed that SDP shall not use pc I or pc/1 as a trademark.

2. pc/1 Professional agrees to secure immediate cancellation of License Agreements with SDP from those licensees listed on the attached list marked as "Exhibit A", by having a cancellation letter executed by each such licensee, which letter shall include the provisions as set forth in the sample letter attached hereto as Exhibit "B". pc/1 Professional further agrees to secure immediate cancellation and/or relinquishment of any and all rights concerning the QS/1 Pharmacy System as are held by G & H Preferred Pharmacy Systems, Limited by having a letter to such effect executed by G & H Preferred Pharmacy Systems, Limited.

3. pc/1 Professional agrees to secure and have returned to SDP all materials in the possession, custody or control of the licensees listed on Exhibit A that have been provided to such licensees by SDP which fall within the provisions of paragraph 12(e) of the License Agreement.

4. SDP agrees to assume responsibility for performance of the duties of the listed licensees with respect to all end users of the QS/1 Pharmacy System in the licensee's respective territories, and to indemnify such listed licensees from any liability concerning maintenance

and upkeep of the QS/1 pharmacy systems of such end users.

5. Upon the successful completion of the obligations of pc/1 Professional set forth in paragraphs 1, 2 and 3 above, SDP agrees to assign in blank its stock in UDA, Inc., its rights to repayment of its load to UDA, Inc., and all monies contingently due SDP as discounts payable from UDA, Inc. for computer sales; provided, however, that the recipient of such assignments from SDP shall upon receipt of same agree to indemnify SDP from any liability whatsoever relating to SDP's stock ownership and/or participation in UDA, Inc., and to hold SDP harmless from any expenses and/or money damages that may result therefrom.

6. SDP agrees to release Hill Pharmacy and pc/1 Professional and their agents, employees, and servants from any and all past and present claims it may have against Hill Pharmacy and/or pc/1 Professional relating from their individual or collective activities relative to the pc/1 pharmacy system.

7. Hill Pharmacy and pc/1 Professional agree to release SDP and its agents, employees, and servants from any and all past and present claims they individually or collectively may have against SDP arising out of any activities of SDP relative to the pc/1 pharmacy system.

8. This agreement represents the entire understanding between the parties, and may not be modified except by an expression in writing signed by all parties.

9. This agreement shall be construed according to the laws of the state of South Carolina.

IN WITNESS WHEREOF, the parties hereto have caused this instrument to be executed by their duly authorized representatives.

Attest:

Witness:

/s/ Dwight Patterson, Jr.

/s/ Betty T. Illegible
Title: Secretary

/s/ Bonnie Hill
Title: Secretary

/s/ Bonnie Hill
Title: Secretary

J M SMITH CORPORATION, d/b/a
SMITH DATA PROCESSING

By: /s/ J M Smith
Title: President

HILL PHARMACY GROUP, INC.

By: /s/ Ken Hill
Title: President

pc/1 PROFESSIONAL SYSTEMS, INC.

By: /s/ Ken Hill
Title: President

EXHIBIT A

W.K. Enterprises
1031 McIntosh Circle Drive
Joplin, Missouri 64801

Professional Systems
1089 N.W. 13th Street No. 9
Boca Raton, Florida 33432

Hill Pharmacy Group, Inc.
300 N. Crockett
Granbury, Texas 76408

Rich-2 Pharmacy Consulting Service
P.O. Box 479
Owego, New York 13827

Preferred Pharmacy Systems
P. O. Box 217
Scottsville, Kentucky 42164

EXHIBIT B

Date: 7-20-83

J M Smith Corporation, d/b/a
Smith Data Processing
P. O. Box 6052
Spartanburg, SC 29304

Re: License Agreement
J M Smith Corporation, d/b/a
Smith Data Processing - ___
Dated ___

Gentlemen:

In order to effectuate a settlement agreement between J.M. Smith Corporation, d/b/a Smith Data Processing, and Hill Pharmacy Group, Inc. and pc/1 Professional Systems, Inc., the undersigned licensee hereby agrees to terminate its aforesaid license agreement for the QS/1 Pharmacy System effective immediately.

Enclosed is our check in the amount of ___ which represents all monies currently owed SDP in conjunction with sales of QS/1 Pharmacy Systems under the aforesaid license agreement.

Also enclosed herewith are all materials which the undersigned licensee is obligated to return to SDP under the provisions of paragraph 12(e) of the aforesaid license agreement, and the undersigned hereby warrants that the enclosed materials represent *all* of any such materials which the undersigned licensee is obligated to return to SDP under the aforesaid agreement.

The undersigned licensee acknowledges that it presently has no claims or rights against SDP as to any commissions or other monies due from SDP relative to

QS/1 pharmacy systems that are or will be employed by end users in the territory specified in the aforesaid license agreement.

Very truly yours,
/s/ Ken Hill